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TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1936

No. 74

AMERICAN TELEPHONE AND TELEGRAPH COMPANY ET AL., APPELLANTS,

vs.

THE UNITED STATES OF AMERICA, FEDERAL COMMUNICATIONS COMMISSION, AND NATIONAL ASSOCIATION OF RAILROAD AND UTILITIES COMMISSIONERS

APPEAL FROM THE DISTRICT COURT OF THE UNITED STATES FOR THE SOUTHERN DISTRICT OF NEW YORK

FILED MAY 22, 1936.

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[fol. 1] [Caption omitted]

[fol. 2]

IN UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

In Equity. No. 81-366

AMERICAN TELEPHONE AND TELEGRAPH COMPANY, NEW ENGLAND TELEPHONE AND TELEGRAPH COMPANY, The Southern New England Telephone Company, New York Telephone Company, New Jersey Bell Telephone Company, The Bell Telephone Company of Pennsylvania, The Diamond State Telephone Company, The Chesapeake and Potomac Telephone Company, The Chesapeake and Potomac Telephone Company of Baltimore City, The Chesapeake and Potomac Telephone Company of Virginia, the Chesapeake and Potomac Telephone Company of West Virginia, Southern Bell Telephone and Telergaph Company, Christian-Todd Telephone Company, The Ohio Bell Telephone Company, The Cincinnati and Suburban Bell Telephone Company, Michigan Bell Telephone Company, Indiana Bell Telephone Company, Wisconsin Telephone Company, Illinois Bell Telephone Company, Northwestern Bell Telephone Company, The Tri-State Telephone and Telegraph Company, Dakota Central Telephone Company, Southwestern Bell Telephone Company, The United Telephone Company, the Mountain States Telephone and Telegraph Company, The Pacific Telephone and Telegraph Company, Southern California Telephone Company, The Home Telephone and Telegraph Company of Spokane and Bell Telephone Company of Nevada, Plaintiffs,

vs.

UNITED STATES OF AMERICA and FEDERAL COMMUNICATIONS COMMISSION, Defendants

BILL OF COMPLAINT—Filed November 22, 1935

To the Honorable the Judges of Said District Court:

Plaintiffs, above named, bring this action pursuant to the provisions of the Communications Act of 1934, approved

[fol. 3] June 19, 1934 (48 Stat. L. 1064, 1093; Code of Laws of the United States, Title 47, Sec. 402 (a)), and of the Urgent Deficiencies Appropriations Act, approved October 22, 1913, (38 Stat. L. 219, 220; Code of Laws of the United States, Title 28, Secs. 41 (28), 43-48, inclusive), to enjoin, set aside, annul and suspend an order of the Federal Communications Commission (hereinafter referred to as the Commission) denominated Telephone Division Order No. 7-C, dated June 19, 1935, effective January 1, 1936, in proceedings entitled:

"In re: Accounting Rules for Telephone Companies, Interstate Commerce Commission Docket No. 25705,"

being Docket No. 2551 of the Commission.

For their cause of action plaintiffs allege:

1. Plaintiff, American Telephone and Telegraph Company, is a corporation duly organized and existing under the laws of the State of New York, having its principal office in the City of New York, State of New York, and in the Southern District thereof. Each of the other plaintiffs above named is a corporation duly organized and existing under the laws of one of the States of the United States. The state of incorporation and the address of each of said other plaintiffs are as follows:

New England Telephone and Telegraph Company, New York, Boston, Massachusetts

The Southern New England Telephone Company, Connecticut, New Haven, Connecticut

[fol. 4] New York Telephone Company, New York, New York, New York

New Jersey Bell Telephone Company, New Jersey, Newark, New Jersey

The Bell Telephone Company of Pennsylvania, Pennsylvania, Philadelphia, Pennsylvania

The Diamond State Telephone Company, Delaware, Philadelphia, Pennsylvania

The Chesapeake and Potomac Telephone Company, New York, Washington, D. C.

The Chesapeake and Potomac Telephone Company of Baltimore City, Maryland, Baltimore, Maryland

The Chesapeake and Potomac Telephone Company of Virginia, Virginia, Richmond, Virginia

The Chesapeake and Potomac Telephone Company of West Virginia, West Virginia, Charleston, West Virginia
Southern Bell Telephone and Telegraph Company, New York, Atlanta, Georgia
Christian-Todd Telephone Company, Kentucky, Hopkinsville, Kentucky
The Ohio Bell Telephone Company, Ohio, Cleveland, Ohio
The Cincinnati and Suburban Bell Telephone Company, Ohio, Cincinnati, Ohio
Michigan Bell Telephone Company, Michigan, Detroit, Michigan
Indiana Bell Telephone Company, Indiana, Indianapolis, Indiana
Wisconsin Telephone Company, Wisconsin, Milwaukee, Wisconsin
Illinois Bell Telephone Company, Illinois, Chicago, Illinois
Northwestern Bell Telephone Company, Iowa, Omaha, Nebraska
[fol. 5] The Tri-State Telephone and Telegraph Company, Maine, St. Paul, Minnesota
Dakota Central Telephone Company, South Dakota, Aberdeen, South Dakota
Southwestern Bell Telephone Company, Missouri, St. Louis, Missouri
The United Telephone Company, Kansas, Abilene, Kansas
The Mountain States Telephone and Telegraph Company, Colorado, Denver, Colorado
The Pacific Telephone and Telegraph Company, California, San Francisco, California
Southern California Telephone Company, California, Los Angeles, California
The Home Telephone and Telegraph Company of Spokane, Washington, Spokane, Washington
Bell Telephone Company of Nevada, Nevada, San Francisco, California

2. The Commission is an administrative tribunal created by the Communications Act of 1934 and is charged with the administration and enforcement of said Act. The Commission was organized on July 11, 1934, and said Act became effective on that date.

3. Each of said plaintiffs is and at all times since the effective date of said Communications Act has been a car-

rier engaged in communication for hire in interstate or foreign commerce, subject to the provisions of said Act.

4. Before and until the enactment of the Communications Act each of said plaintiffs was a common carrier engaged in the transmission of intelligence for hire in interstate [fol. 6] commerce and was subject to the jurisdiction of the Interstate Commerce Commission under the provisions of the Interstate Commerce Act as amended. Each of said plaintiffs was such a carrier subject to said jurisdiction at all times subsequent to a date prior to January 1, 1913, except the following named plaintiffs, each of which was such a carrier subject to said jurisdiction at all times subsequent to the date set opposite its name:

Bell Telephone Company of Nevada	February 1, 1913.
Chesapeake and Potomac Telephone Company of West Virginia	January 1, 1917.
Southern California Telephone Company	May 1, 1917.
Indiana Bell Telephone Company	April 1, 1920.
The Ohio Bell Telephone Company	September 21, 1921.

The Interstate Commerce Commission, pursuant to the authority vested in it as aforesaid, entered an order dated December 10, 1912, prescribing for certain telephone companies, including plaintiffs, a uniform system of accounts entitled "Uniform System of Accounts for Telephone Companies, First Issue," effective January 1, 1913, as to such of plaintiffs as were then subject to its jurisdiction and effective as to the remainder of plaintiffs when they became subject thereto. Said system was amended in minor respects by subsequent orders dated December 22, 1914, July 24, 1923, January 8, 1925 and December 19, 1927. By [fol. 7] a further order dated November 12, 1932, said Interstate Commerce Commission prescribed for certain telephone companies, including each of said plaintiffs, a revised system of accounts entitled "Uniform System of Accounts for Telephone Companies, First Revised Issue," effective January 1, 1933.

Compliance with the said orders was obligatory upon each of plaintiffs at all times during which it was a common carrier subject to the Interstate Commerce Act, as above alleged, and compliance with said order of November 12, 1932, is now obligatory upon all of them, and plaintiffs are

prohibited by law from keeping any other or different accounts than those so prescribed. At all times subsequent to the respective dates on which each of said plaintiffs became a common carrier subject to said Interstate Commerce Act, as above alleged, its accounts have been kept and are now kept in full compliance with said orders, as required by law.

5. The Interstate Commerce Commission, in response to the request of certain state commissions, entered a further order dated December 27, 1932, for a public hearing with respect to said "First Revised Issue, said case being identified as "Docket No. 25705, Accounting Rules of Telephone Companies." Hearings were thereafter duly held before the Interstate Commerce Commission in April, and again in June, 1933, and on July 9, 1934, said Interstate Commerce [fol. 8] Commission issued a report setting forth its findings and conclusions upon the various exceptions and proposed amendments presented at said hearings. A copy of said report is hereto attached, marked Exhibit A, and made a part hereof.

Jurisdiction of said pending proceeding was thereafter and on July 11, 1934 transferred to the defendant, Federal Communications Commission, by virtue of the provisions of Section 604 (b) of the Communications Act. The Commission proceeded therein and on August 16, 1934, issued Telephone Division Order No. 7 notifying state commissions and other parties in interest that they might file exceptions or objections to the said report of the Interstate Commerce Commission or suggest amendments to such accounting rules, the case being redocketed and identified as Federal Communications Commission Docket No. 2551. A hearing was thereafter held on November 16, 1934. Thereafter and on May 1, 1935, the Commission issued Telephone Division Order No. 7-B setting forth a proposed Uniform System of Accounts for Telephone Companies entitled "Issue Effective January 1, 1936," and therewith a notice to all parties, including plaintiffs, that they might file exceptions thereto for consideration by the Commission at a conference with the parties, which was held on May 16, 1935.

Thereafter, on June 19, 1935, the Commission issued the [fol. 9] order complained of in this suit, designated Telephone Division Order No. 7-C, prescribing, for the use of telephone companies subject to said Act and having aver-

age annual operating revenues exceeding $50,000.00, a system of accounts entitled "Uniform System of Accounts for Telephone Companies, Issue of June 19, 1935, Effective January 1, 1936," and requiring every such carrier to keep all accounts in conformity therewith on and after January 1, 1936. A copy of said Order No. 7-C, including the text of said "Issue of June 19, 1935" prescribed thereby is hereto attached, marked Exhibit B, and made a part hereof. Plaintiffs are telephone companies having average annual operating revenues exceeding $50,000.00.

6. Said Order No. 7-C is unlawful and void in that it is contrary to Section 404 of said Act and in violation of the rights of plaintiffs under the due process clause of the Fifth Amendment to the Constitution of the United States, for the reason that in said proceeding and investigation the Commission made no report in writing, no findings and no statement of its conclusions.

7. Said system of accounts prescribed by said Order No. 7-C requires plaintiffs to record their properties upon their books of account and records at their "original cost" which is defined in said system as "the actual money cost of (or the current money value of any consideration other than money exchanged for) property at the time when it was first dedicated to the public use, whether by the accounting company or by a predecessor public utility."
[fol. 10] Portions of plaintiffs' property have been acquired by them from other public utility companies, and in many cases those companies had acquired such property from still other public utility companies. Practically all such property which is now in existence has been acquired subsequent to January 1, 1913 and a large part thereof has been recorded in plaintiffs' property investment accounts at its actual cost to the plaintiffs, the remainder being recorded by a merger of book accounts or at current cost new, all as required or permitted by the Interstate Commerce Commission. Such property is of substantial value.

The aforesaid definition of "original cost," taken in connection with other provisions of said system of accounts, will require in substance and effect.

That as of January 1, 1936, plaintiffs shall restate their then existing property investment accounts by eliminating therefrom the recorded cost or investment of plaintiffs in

property theretofore acquired by them from another public utility, and substituting for such recorded cost or investment the amount (estimated if not known) which said property cost some former owner at the date of first dedication to public use.

That any property acquired by plaintiffs from another public utility on or after January 1, 1936, shall be included in their property investment accounts, not at the amount plaintiffs actually pay therefor, but at the amount which [fol. 11] some prior owner had paid therefor at the date of first dedication to public use.

That plaintiff shall segregate in an account numbered 100.4 and entitled "Telephone Plant Acquisition Adjustment," the difference between the recorded cost of their property so acquired (or the actual cost where acquired after January 1, 1936) and the cost of said property to the prior owner who first devoted it to the public use, and that the amounts recorded in this account shall then be disposed of, written off or amortized as the Commission shall direct.

That plaintiffs shall record nothing in their accounts on account of the expense of depreciation with respect to the portion of their property investment which is to be recorded in Account 100.4, "Telephone Plant Acquisition Adjustment."

The foregoing requirements are so entirely contrary to fundamental principles of correct accounting and so arbitrary and unreasonable as to amount to an abuse of the Commission's power, are beyond the statutory power and authority of the Commission, and are illegal and void, for the following reasons:

(a) They require plaintiffs' property investment accounts to be kept on a basis which will reflect neither the fact of their actual investment in their property nor the value thereof, but which will conceal the amount of plain- [fol. 12] tiffs' actual investment and will substitute therefor, in the case of purchased property, the investment of some one else (estimated if not known) for which plaintiffs had no responsibility. The accounting will thus conceal relevant facts and misrepresent plaintiffs' condition.

(b) Where plaintiffs have heretofore purchased property at a price higher than its cost to the predecessor utility which first dedicated it to the public use, they require plain-

tiffs to write off a portion of their actual investment, even where the price paid was the actual value of the property and where there has been no change in value, thus requiring them to record a loss on their books when in fact they have suffered no loss. A similar writing off of a loss which has not been incurred will be required of plaintiffs whenever in the future they may purchase property at a price which, although representing its actual value, is higher than its cost to the predecessor public utility which first dedicated it to the public use.

(c) They prevent plaintiffs from recording in their expense accounts the expense of depreciation which they actually incur.

(d) Said requirements are impracticable of application in plaintiffs' accounting. They would necessitate establishing the identity of items of purchased property many years after the purchase, when many of the purchased items had [fol. 13] been retired and when the surviving items had become so commingled with previously owned and subsequently constructed plant that their identification would be impossible. They would necessitate estimating the "original cost" and the dates of installation of such items, because the books and records of the company first devoting the property to public use are in many cases not available, and because in many other cases such books and records were not kept in such a manner as to show such "original cost" or such dates of installation. Such estimates would in most cases be impossible to make except by mere guesswork. They would necessitate the separation of plaintiffs' investment in a single item of purchased property into two accounts, and when it became necessary, on retirement of that item, to write it out of the accounts, there would be no practical way of distinguishing items which had been charged to the two accounts from commingled nonpurchased items of the same kind which had been charged to only one account. These difficulties would add greatly to the accounting expense of plaintiffs and would result in their accounts reflecting, in part, unreliable estimates instead of facts.

(e) Said requirements compel plaintiffs to make radical changes in their completed accounts. The Communications Act does not empower the Commission to prescribe

[fol. 14] retroactive changes in accounts which have been lawfully and correctly kept, but only to prescribe the forms of accounts, records and memoranda to be kept in the future.

(f) They require the amounts recorded in Account 100.4, "Telephone Plant Acquisition Adjustment," to be disposed of, written off or amortized by plaintiffs, not in accordance with any accounting rule or classification prescribed by the Commission as a part of said system of accounts or otherwise, but in such manner as the Commission may direct as to each individual property acquisition. The Commission's authority is limited to the making of rules, regulations and classifications, in accordance with which all carriers within a class must keep their accounts or suffer the penalties prescribed by the Act. It has no authority to issue an individual order requiring an individual carrier to make such specific accounting entry as it may direct with respect to a transaction as to which it has made no accounting rules, regulations or classifications.

(g) Said requirements are inconsistent with and contrary to Sections 213 (c) and 219 (a) of said Act, and in violation of Section 4 (i) thereof, and bear no reasonable relationship to the ends and purposes for which the Commission is authorized by said Act to prescribe the forms of accounts to be kept by carriers subject thereto.

[fol. 15] 8. Said system of accounts requires that where plaintiffs purchase from another public utility, property which was donated to such public utility, plaintiffs shall record as a liability, in an account entitled "Contributions of Telephone Plant," the amount of the donation to the prior owner. To thus require plaintiffs' accounts to show a liability for a contribution which plaintiffs have not received is arbitrary and unreasonable, beyond the statutory power and authority of the Commission and therefore illegal and void.

9. Said system of accounts requires plaintiffs to include a part of their investment in property in Account 100.1, "Telephone Plant in Service," a part in Account 100.3, "Property Held for Future Telephone Use" and a part in Account 103, "Miscellaneous Physical Property." The dividing lines between these classifications, as stated in said

system of accounts, are so indefinite and ambiguous that it will be impossible for plaintiffs to know to which account substantial amounts of their property should be charged. Plaintiffs will of necessity be required to make entries in these accounts at their peril, at the risk of the penalties prescribed by said Act. The Commission is without authority to prescribe such classifications and the exaction of obedience to rules so vague and indefinite is in violation of the rights of plaintiffs under the Fifth and Sixth Amendments to the Constitution of the United States, which require due process of law and that persons accused of crime [fol. 16] shall be adequately informed of the nature and cause of the accusation.

10. The nature of plaintiffs' business is such that a portion of their property during periods of its life necessarily constitutes what is known as spare plant. Said system of accounts requires that such property be included in Account 100.3, "Property Held for Future Telephone Use," during such periods. Said system also requires the computation of depreciation expense at rates based on the entire life of the property, including the portion of its life during which it is included in Account 100.3, but prevents the recording of any depreciation expense with respect to such property during the period in which it is included in Account 100.3. The result is that plaintiffs will be prevented from recording on their books the full expense of depreciation with respect to property which, during any portion of its life, is included in Account 100.3, "Property Held for Future Telephone Use." The said requirements are contrary to the fundamental principles of correct accounting, arbitrary and unreasonable, and are therefore illegal and void.

11. Said system of accounts requires that all charges to plant investment, income, operating revenue and operating expense accounts shall be just and reasonable and that any payments by plaintiffs in excess of such just and reasonable charges shall be charged against income. This re- [fol. 17] quirement is contrary to the fundamental principles of correct accounting, arbitrary and unreasonable, in that it will require the accounts to record judgment as to what should have been spent, instead of the fact of what was spent, and for the further reason that the words "just and

reasonable'' in their context are vague, lacking in precise definition and susceptible of a wide variation of opinion, so that it will be impossible for plaintiffs to know to what account their expenditures should be charged. Plaintiffs will of necessity be required to make all charges to these accounts at their peril, at the risk of the penalties prescribed by said Act. The Commission is without authority to prescribe such a requirement and the exaction of obedience to a rule so vague and indefinite is in violation of the rights of plaintiffs under the Fifth and Sixth Amendments to the Constitution of the United States, which require due process of law and that persons accused of crime shall be adequately informed of the nature and cause of the accusation.

12. It is necessary that the plaintiffs keep books of account which will accurately record the facts of their transactions and which will truly reflect their actual condition, for the information of their officers and directors, so that they may intelligently manage the business, may make accurate reports to taxing authorities and other governmental agencies, and may make true representations to prospec- [fol. 18] tive investors, as well as for the information of their existing stockholders and other security holders. The accounts of plaintiffs as heretofore and at present kept have been and are adequate for such purposes. The order complained of makes it impossible for plaintiffs to keep accounts adequate for any of such purposes, but will require plaintiffs' accounts to conceal relevant facts and to misrepresent their true condition, to plaintiffs' serious damage.

Plaintiffs have for many years filed with governmental agencies and issued to investors and to the public financial statements taken from their books of account as heretofore kept, and said books of account have formed the basis of their corporate financing and of many other matters affecting their very existence. The order complained of would result in the publication of financial statements radically different from those heretofore issued. The enforced publication of statements which would contradict those on which plaintiffs' entire financial structures have been based would seriously impair plaintiffs' credit, and thus take their property without due process of law in violation of

the Fifth Amendment to the Constitution of the United States.

13. Said "Issue of June 19, 1935," purports to constitute a complete system of accounts; its provisions are interdependent and nonseverable, and it is impossible practically and legally to separate the provisions which effectuate the [fol. 19] illegal requirements hereinabove set forth from the other provisions thereof. Said "Issue of June 19, 1935," and said Order No. 7-C prescribing the same, are therefore illegal and void in their entirety, upon all the grounds hereinabove alleged.

14. Said Order No. 7-C requires plaintiffs, during the year 1936, to keep not only the complete system of accounts prescribed thereby, but also such portion or portions of their present accounts as may be necessary for comparison of 1936 results with results of previous years. The changes in plaintiffs' accounting required by said Order No. 7-C affect so many of plaintiffs' present accounts that compliance with the above requirement would compel plaintiffs, at great expense, to keep almost a complete set of accounts in accordance with the present system in addition to a complete set of accounts in accordance with the system prescribed by said order. The said requirement is arbitrary and unreasonable, beyond the statutory power and authority of the Commission, and therefore illegal and void.

15. In the premises, plaintiffs have no adequate remedy at law, and unless the relief prayed for herein be granted to plaintiffs, they will suffer, for the reasons and in the manner stated in this Bill of Complaint, irreparable injury and damage.

[fol. 20] 16. Plaintiffs are advised and therefore allege that unless said order of the Commission and said system of accounts prescribed thereby are complied with on and after January 1, 1936, or unless prior to that date plaintiffs are afforded the protection, by a writ of injunction, which this court alone is competent to grant, they and their officers and employees will, under the terms of the Communications Act of 1934, and particularly under Sections 220, 501 and 502 thereof, be subjected to a multiplicity of suits and criminal prosecutions for the recovery and assessment

of the fines and penalties in said sections provided. If said order and said system of accounts prescribed thereby are enjoined, set aside, annulled and suspended as hereinafter prayed, plaintiffs will be required to continue keeping all their accounts, records and memoranda in accordance with the system of accounts entitled "Uniform System of Accounts for Telephone Companies, First Revised Issue," prescribed by an order of the Interstate Commerce Commission dated November 12, 1932, effective January 1, 1933, which is still in full force and effect, and which will remain in full force and effect by virtue of Section 604 (a) of said Communications Act until rescinded or superseded by a valid order of the Federal Communications Commission.

Wherefore, plaintiffs pray:

(1) That a subpoena or subpoenas in chancery issue out of or under the seal of this Honorable Court directed to [fol. 21] the defendants as required by law, and that due and proper service of such process and of this Bill of Complaint be forthwith made by filing a copy thereof in the office of the Secretary of the Commission and another copy in the Department of Justice as in said Urgent Deficiencies Appropriations Act provided, and that thereby the defendants and each of them be required on or before a date to be specified in such subpoena or notice, to appear herein and answer this Bill of Complaint, but not under oath, answer under oath being expressly waived.

(2) That the court, as soon as practicable, convene a specially constituted court of three judges, as required by Title 28, Section 47, Code of Laws of the United States, and that a temporary or interlocutory injunction be entered herein, restraining, enjoining and suspending, until the further order of this court, the operation, execution, effect and enforcement of said order of the Commission.

(3) That pending a hearing upon the aforesaid application for a temporary or interlocutory injunction a preliminary restraining order be issued in terms restraining, enjoining and suspending the operation, execution, effect and enforcement of said order of the Commission until said application for a temporary or interlocutory injunction shall have been heard and determined.

(4) That after final hearing this court adjudge, order and decree that said order of the Commission is and has [fols. 22 & 23] at all times been beyond the lawful authority of the Commission, in violation of the legal rights of plaintiffs, and wholly void; and that said order be perpetually vacated, set aside, suspended, and annulled, and the enforcement thereof perpetually restrained and enjoined.

(5) That plaintiffs may have such other and further relief in the premises as to equity and justice may appertain and as may be deemed by this Honorable Court to be adequate and proper under the circumstances.

C. M. Bracelen, Chas. T. Russell, Alan J. McBean, Solicitors for Plaintiffs, Address: 195 Broadway, New York, New York.

Duly sworn to by Charles P. Cooper. Jurat omitted in printing.

19766

INTERSTATE COMMERCE COMMISSION

No. 25705

ACCOUNTING RULES FOR TELEPHONE COMPANIES

Submitted June 15, 1933. Decided July 9, 1934

Questions respecting revisions of the Uniform System of Accounts for Telephone Companies, First Revised Issue, proposed by regulatory commissions of certain States and the District of Columbia, considered and determined. Certain revisions adopted as proposed and others modified and adopted. Certain provisions of the system of accounts construed. Effective dates, as originally fixed, retained.

Mason M. Patrick, *Riley E. Elgen*, and *William A. Roberts* for Public Utilities Commission of District of Columbia; *J. F. Harper* for Public Service Commission of Maryland; *Mayland H. Morse* and *H. Styles Bridges* for Public Service Commission of New Hampshire; *Milo R. Maltbie*, *Charles G. Blakeslee*, and *Malcolm Orton* for Public Service Commission of New York; *Paul A. Walker*, *A. H. Baldridge*, and *P. R. Reed* for Corporation Commission of Oklahoma; *Frederick P. Gruenberg* for Public Service Commission of Commonwealth of Pennsylvania; *E. K. Murray* for Department of Public Works of Washington; *David E. Lilienthal*, *J. H. Bickley*, and *Geo. C. Mathews* for Public Service Commission of Wisconsin; *John Bernhard* for Board of Public Utility Commissioners of New Jersey; *Clyde S. Bailey* and *John E. Benton* for Arizona Corporation Commission, Nebraska State Railway Commission, Public Service Commission of Nevada, and Public Utilities Commission of Utah; *R. O. Self* for North Carolina Corporation Commission; and *D. E. Brisbine* for Board of Railroad Commissioners of State of South Dakota.

Harvey Hoshour and *A. J. McBean* for American Telephone and Telegraph Company and associated companies, and *Edward W. Beattie* for New York Telephone Company.

F. B. MacKinnon and *Alfred L. Geiger* for United States Independent Telephone Association.

REPORT OF THE COMMISSION

BY THE COMMISSION:

This proceeding grows out of objections to our Uniform System of Accounts for Telephone Companies, First Revised Issue, herein referred to as the uniform system, promulgated November 12, 1932, in accordance with section 20 of the Interstate Commerce Act, and

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effective January 1, 1933, and January 1, 1934, for class A and class B companies, respectively.

These objections were interposed by Railroad Commission of the State of California, Public Utilities Commission of the District of Columbia, Public Service Commission of Maryland, Public Service Commission of Missouri, Public Service Commission of New Hampshire, Public Service Commission of New York, Corporation Commission of Oklahoma, the Public Service Commission of the Commonwealth of Pennsylvania, Department of Public Works of Washington, Public Service Commission of Wisconsin, Public Utilities Commission of Maine, Board of Public Utility Commissioners of New Jersey, the Public Utilities Commission of Ohio, Public Utilities Commissioner of Oregon, the Railroad Commission of South Carolina, State Corporation Commission of Virginia, Arizona Corporation Commission, Nebraska State Railway Commission, Public Service Commission of Nevada, Public Utilities Commission of Utah, Minnesota Railroad and Warehouse Commission, North Carolina Corporation Commission, and Board of Railroad Commissioners of the State of South Dakota, hereinafter referred to by groups, or individually by prefixing the name of State or District, or generally as the State commissions.

A hearing has been held and the matter was submitted without briefs. Following its submission, consideration of the matter was delayed, owing largely to the fact that the commissioner who had been given administrative charge of the proceeding was designated by the President as Federal Coordinator of Transportation under the Emergency Railroad Transportation Act, 1933. In the meantime an act has become effective (Public No. 416, 73d Congress) relieving this Commission from its duties with respect to telephone and telegraph companies and transferring jurisdiction over these and other companies to the newly created Federal Communications Commission. At this date, the latter commission has not been organized, but there is every prospect that it will be organized before the expiration of the 30 days which must elapse before any order that we might issue could become effective. We are, therefore, not in a position to enter an order. In fairness to the new commission, however, we believe that we should adopt this report, in order that it may be advised of our views upon the record made in a proceeding which we instituted. It seems desirable, also, that the report should be issued in such form that the new commission may readily be able to supplement it by an order, if that be deemed desirable. For convenience, the report is written as if our jurisdiction were to continue.

Our order of December 27, 1932, granting a hearing herein, provided that if as a result thereof it should be found necessary to modify the uniform system in any particular the modifications would become effective as of January 1, 1933. During the course of the hearing the Bell system companies stated that this would prove burdensome in the event of substantial revision, and urged that such provision be vacated. Inasmuch as the matter is related to the extent and nature of such modifications as may be found to be necessary, it will be disposed of in the statement of our general conclusions at the close of the report.

It appearing that the presentation on behalf of the State commissions would be in the nature of argument, the presiding commissioner announced at the opening of the hearing that none of those who participated would be sworn, but that they would be subject to interrogation by all interested parties.

The chairman of the New York Commission presented, on behalf of the first 10 State commissions above named, hereinafter referred to as the 10 commissions, a memorandum of objections to provisions of the uniform system, concluding with a motion for rescission thereof and the incorporation of the modifications sought in the event a further revised system of accounts should be promulgated. Counsel for the State commissions of Arizona, Nebraska, Nevada, and Utah announced that they joined in the foregoing. It is not conceded by any of this group that we have jurisdiction over telephone depreciation rates.

The major portion of the objections presented in this memorandum, and presumably all that were deemed of sufficient importance, were subsequently covered by the specific recommendations hereinafter considered.

The memorandum was prefaced by directing attention to the following: That our jurisdiction with respect to telephone companies does not include all aspects of regulation; that the activities of telephone companies as measured by revenues are predominantly intrastate; that the jurisdiction of many of the State commissions with respect to telephone companies is general in scope; that by reason of limitations affecting some State commissions and the shortness of notice of the effective date of the uniform system they were prevented during 1933 from prescribing accounting systems or requiring the keeping of the necessary subsidiary accounts; that the uniform system interferes with the exercise of jurisdiction on the part of State commissions concerning matters over which we have no jurisdiction; that it accords little recognition to the powers and duties of the State commissions regarding telephone companies; and that in the many

instances where matters are required to be submitted for our approval and authorization, it omits subjecting them also to the approval of the State commissions.

In the measures adopted with respect to the uniform system, we are acting in pursuance of the direction of Congress. Uniformity is the desired and important object. The nature of the undertaking necessarily precludes the incorporation of special provisions covering the requirements of the several State commissions.

We have, however, recognized the needs of the several State commissions in the intrastate regulation which is their duty and have endeavored to help them in the securing of all necessary information by leaving it open to them to require subdivision of the accounts prescribed. To go further would interfere with the uniformity of accounting which is essential to the proper exercise of our own jurisdiction.

Although invited by the presiding commissioner, no definite comment was offered by the State commissions touching the desirability of providing for segregation of the costs of services rendered to other companies, with respect to which the payment received is includible in account 525, "Revenues from general services and licenses."

The representative of the 10 commissions also presented on behalf of the Missouri commission, a supplemental memorandum emphasizing certain objections embodied in the principal memorandum and containing others relating to matters subsequently covered by proposed revisions introduced of record. The memorandum also suggested subdivision of various accounts. Since the Missouri commission was a party to the specific recommendations hereinafter discussed, we shall treat the latter as covering the matters upon which substantial reliance is placed.

The District of Columbia commission urges, as special grounds for our rescission of the uniform system, that it has jurisdiction over the accounts and depreciation rates of telephone companies operating within said district, which jurisdiction emanates from the same authority as does our own, respecting telephone companies subject to the Interstate Commerce Act; that with respect to said district, Congress is empowered to enact what is expressly described in the Constitution as "exclusive" legislation, whereas the power to regulate commerce among the several States is not so described; that the act of March 4, 1913, from which its powers over such accounts are derived is mandatory in form, whereas section 20 (5) of the Interstate Commerce Act (reenacted February 28, 1920) is merely permissive with respect to accounts; and that the later of these two

statutory provisions does not repeal the earlier, because repeals by implication are not favored.

The District of Columbia commission seems to content itself with invoking our discretion to rescind the uniform system, and it will be noted from the foregoing that its position is essentially one of defense of its own jurisdiction rather than direct attack on ours. We shall, however, first consider the grounds stated in their broader aspects.

The first ground is only of importance in the event the last is valid, and the others are mere aids to the last. We do not see that the difference in wording of the respective powers of Congress concerning said district and concerning interstate commerce, or of the respective acts thereunder conferring authority to regulate accounts, leads to the conclusion that the former should prevail over the latter. Moreover, regardless of whether the act relied upon may have been repealed by implication, the force of that portion of the subsequent statute from which our jurisdiction flows is clearly not impaired by reason of repugnancy with the prior one.

Dealing now with the point that is pressed, it will suffice to say that as early as December 10, 1912, we exercised our discretion to promulgate a uniform system of accounts for telephone companies effective January 1, 1913, and this remained in effect until superseded by the uniform system herein. We regard the importance of uniformity in accounting as paramount to any of the considerations urged and perceive no sufficient reason at this late date for recalling the exercise of our discretion in that respect. Furthermore, the questions involving depreciation accounting and rates were necessarily involved in *Telephone and Railroad Depreciation Charges*, 177 I.C.C. 351, hereinafter referred to as the *Depreciation case*, and the notice setting the date for hearing the instant proceeding expressly stated that the *Depreciation case* had not been reopened and that this hearing was not for the purpose of reconsidering the findings and orders therein.

The Wisconsin commisson separately reserved the point that with respect to intrastate operations of telephone companies its jurisdiction over depreciation rates is exclusive and that we have not and could not constitutionally be vested with jurisdiction thereover. Counsel for the Wisconsin commission also reserved, on behalf of the first 21 State commissions above named, hereinafter referred to as the 21 commissions, the point that we have no jurisdiction to regulate telephone accounting except as to interstate operations. Of course, in promulgating the uniform system we have necessarily held that we had jurisdiction to do so. See also *Accounting of New York Telephone Co.*, 188 I.C.C. 83, 84, 85.

The New Jersey commission, while joining in the objections of the 10 commissions, expressly reserved the point that we have not, and could not constitutionally, be vested with jurisdiction so to act as to qualify its authority over intrastate operations of telephone companies.

Prior to the promulgation of the uniform system we sought the cooperation of the State commissions by sending them copies of all tentative drafts and inviting comment and criticism with reference thereto. The matter was also the subject of conferences with the State commissions and with the telephone companies. Such suggestions as were received were carefully considered and as a result changes were made.

Upon the suggestion of the presiding commissioner and in accordance with the offer contained in the memorandum of objections, the 14 State commissions parties thereto announced that they would supplement this memorandum by filing and serving upon interested parties a specific statement of proposed revisions of the uniform system designed to carry into effect their recommendations.

Thereafter and pursuant to the foregoing, the first 16 State commissions above named served and filed a statement of concrete recommendations in which the State commissions of Arizona, Nebraska, Nevada, Utah, and Minnesota also joined.

As filed and incorporated in the record, most of the proposed additional provisions are not numbered. Since the blanks thus left in the statement of recommendations have a tendency to render the matter somewhat unwieldy, we have interpolated numbers shown in brackets for purposes of identification and cross reference. For convenience we have also assigned numbers prefixed by "R" to the several proposed revisions or parts thereof.

These recommendations, including others subsequently added, and various amendments which have been incorporated, as indicated, are as follows:

[R–1] Page VI of the order. In the fifth ordering clause change "may" to "shall"; insert in the third line after "prescribed" the words "in the manner ordered by any state commission having jurisdiction or"; insert "such" before "commission"; and strike out "having jurisdiction."

[R–2] Instruction 2. Records. In paragraph (C) (2) add at the end "or when required to be kept by a state commission having jurisdiction."

[R–3] In paragraph (C) (3) add after "etc." "or in obedience to the requirements of a state commission having jurisdiction."

[R–4] Insert a new paragraph, (D) [(E)], as follows:

D. [(E)] "The forms of statements for balance sheet accounts, telephone plant accounts, income accounts, surplus accounts, operating revenue accounts, and operating expense accounts, as set forth herein, shall not be construed as preventing any state commission having jurisdiction from requiring the use of different forms for such statements in reports to it, nor from requiring that subdivisions of the prescribed accounts be shown in such statements."

[R–5] Insert a new instruction to follow present instruction 2, to read as follows:

[2.1 Submission of journal entries, etc. –] In all instances where provision is made herein for the submission of proposed journal entries or questions, or for the obtaining of the approval of this Commission, the matter shall be submitted in the first instance to the state commission, if there is such a commission having jurisdiction either directly through the authority to prescribe a classification of accounts or indirectly through authority to prescribe the accounting therefor as a condition to its approval of proposed mergers, purchases, security issues, or other matters. The decision of such commission shall be forwarded to this Commission by the company, with a statement whether or not the company accepts such decision and, if not, the reasons why in its opinion the accounting prescribed in such decision is in conflict with this system of accounts, and a copy of such statement shall also be filed with such state commission.

[R–6] Instruction 3, Definitions. (D) Affiliated Companies. Insert an additional item (A) (6) [(a) (6)] as follows:

(6) "Ability to control the action of the company with or without the major part of the voting power in the controlled company".

[R–7] In paragraph (E) insert the word "gross" before "amount"; and insert "without deduction of related reserves." at end.

[R–8] In paragraph (J), definition of "depreciation", insert at the end the words "Included in the causes are wear and tear, decay, action of the elements, casualties, inadequacy, obsolescence, changes in the art, changes in demand and requirements of public authorities."

[R–9] [Additional] Instruction 3, Definitions. Insert after paragraph (S) a definition as follows:

[S.1] "'Original cost' means the actual money cost (or the current money value of any consideration other than money) of property at the time when it was first devoted to the public service whether by the accounting company or by a predecessor public utility."

[R–10] In paragraph (V), definition of "replacing" and "replacement", strike out the words "and recovery".

[R–11] Strike out period at end of definition (BB) and add "for its use within one year from date of acquisition."

[R–12] Instruction 14, Discount and premium on capital stock. Insert in paragraph (C) after the word "permitted", the words "by the state commission".

[R–13] Instruction 20, Purpose of telephone plant accounts. In paragraph (A) insert the word "original" before the word "cost" in line 3.

[R–14] In the same paragraph insert "within one year" after the word "service" in line 7.

[R–15] In the same instruction in paragraph (B), strike out the words "paragraph (C) in this instruction and" and strike out paragraph (C) and the note following it.

[R–16] [As amended.] Instruction 21, Telephone plant purchased. Strike out (1), (2), (3), (4), and (5) of paragraph (B) and insert:

(1) There shall be charged to account 276, "Cost of telephone plant purchased", the purchase price to the accounting company of the plant purchased.

(2) There shall then be credited to account 276, "Cost of telephone plant purchased", the purchase price to the accounting company of the plant purchased. Concurrently, there shall be charges to the primary telephone plant accounts, and to account [100.1], "Construction work in progress", for the original cost of construction and installation of such plant, and for the original cost of the governmental franchises and similar rights and of land acquired. If the actual original cost is not known, the charges to the primary plant accounts shall be based upon estimates of such cost.

(3) The amount of the reserve requirements applicable to the plant shall be credited to accounts 171, "Depreciation reserve", and 172, "Amortization reserve", and the amount in account [175], "Contributions for extensions", on the books of the vendor, applicable to the property purchased, shall be credited to such account. If not known, such amounts shall be estimated.

(4) The credit to account 276, "Cost of telephone plant purchased", and the charges to primary plant accounts, and to account [100.1] "Construction work in progress", and the credits to the amortization and depreciation reserves and to account [175], "Contributions for extensions", shall be accompanied by a debit or a credit to account [100.2], "Telephone plant purchase adjustment", for the difference between (a) the cost to the accounting company of the telephone plant purchased; and (b) the actual original cost of the construction and installation of such plant, of the governmental franchises and similar rights acquired, and of land acquired, less the amount or amounts credited to the depreciation and amortization reserves and account [175], "Contributions for extensions". The entries to account [100.2], "Telephone plant purchase adjustment", may be subdivided according to the character of the amounts contained therein.

(5) When any purchased plant includes duplicate or other telephone plant which will be retired by the purchaser in the reconstruction of the purchased property and its consolidation with previously owned property, the accounting for the amount applicable to such plant shall be presented to this Commission for consideration and approval.

(6) To be the same as present paragraph (E) of this construction.

[R–17] Strike out paragraph (C) of this instruction and substitute for it the following:

(C) There shall be submitted to this commission the following information:

(1) Journal entries recording the purchase and accounting distribution of a complete telephone system, a complete exchange or a complete toll system. The text of such entries shall give a complete description of the property purchased and the bases upon which the amounts of the entries have been determined.

(2) A copy of the contract of purchase.

(3) A detailed statement showing the original cost of construction and installation of property set up by the prescribed telephone plant accounts, or the estimate of the original cost of the property if such estimate is necessary, together with the reasons for such estimate.

(4) A computation of the reserve requirements for depreciation and amortization.

(5) A detailed statement of the amounts, by primary accounts, carried by the vendor with respect to the property acquired, together with the amounts carried by the vendor in the depreciation and amortization reserves and in the plant contributions account with respect to the property.

(6) A copy of the inventory and appraisal, if one, of the property purchased.

(7) A copy of the order or orders made by a state commission in connection with such purchase.

Strike out paragraph (D) of this instruction.

Strike out paragraph (F) of this instruction.

[R–18] *Instruction 22, Cost of construction.* Insert at the end of line 8 of paragraph (A) the words "employees' pensions and benefits", and after the word "insurance" in line 5 the words "construction services,".

[R–19] At the end of paragraph (B) (4) insert the words "separate records shall be kept and separate charges made for such work performed by affiliated companies".

[R–20] In paragraph (B) (10) (b) insert after the word "debt" in line 4 the words ", less interest earned on such funds,"; and add at the end of this paragraph the words "The amounts to be thus included in the cost of telephone plant shall not be in excess of a reasonable rate of interest."

[R–21] Strike out the first sentence of paragraph (B) (10) (c) and substitute for it the following:

(c) Unless specifically authorized by the state commission having jurisdiction and by this Commission, no interest shall be charged prior to actual construction of the property concerned, nor shall interest be charged during a period of suspension of construction exceeding one year.

[R–22] Insert a new instruction following present instruction 22, as follows:

[22.1] Overhead construction costs.

(A) All overhead construction costs, such as engineering, supervision, general office salaries and expenses, construction engineering and supervision by others than the accounting company, law expenses, insurance, injuries and damages, employees' pensions and benefits, taxes and interest, shall be charged

to particular jobs or items on the basis of the amounts of such overheads applicable thereto, to the end that each job or item shall bear its proper share of such cost and that the entire cost of the item, both direct and indirect, shall be deducted from the plant accounts at the time the item of plant is retired.

(B) The records supporting the entries for construction overheads shall be so kept as to show the nature of expenditures, the individual jobs and accounts charged with each kind of overhead cost, and the bases of the distribution. The amounts charged to each plant account for each overhead shall be available without detailed analysis.

(C) The instructions contained herein shall not be interpreted as permitting the addition to plant accounts of arbitrary percentages or amounts to cover assumed overhead costs, but only as requiring the assignment to particular jobs and accounts of actual and necessary overhead expenditures.

[R–23] [As amended.] Instruction 25. Telephone plant retired. Insert a new paragraph to read as follows:

[aA] To the end that the telephone plant accounts shall at all times disclose the cost of all property in service, the cost of retired property, whether replaced or not, except as provided in paragraph B–2, [(A)(2)] below, must be credited to the account or accounts in this classification to which such cost was charged. Every company should, therefore, take such measures and establish such procedure as will insure strict compliance with these requirements. When anything is worn out, lost, sold, destroyed, abandoned, surrendered upon lapse of title, becomes permanently unserviceable or is withdrawn or retired from service for any other reason, the amount at which such thing stood charged in the plant account shall be credited to the appropriate plant account, and the entry of such credit shall cite by name and page of book or other record the original entry of cost of the thing retired. If there is no original entry that fact shall be stated in connection with the credit entry. If the amount originally charged is not separately recorded, it shall be taken to be the proportionate share of said property in the book cost of the entire group in which the property is included.

[R–24] In present paragraph (A)(2) of this instruction in line 17, strike out the word "or" and insert comma; and insert after the word "capacity" the words "or more economical in operation".

[R–25] In present paragraph (C) of this instruction in lines 7–8 strike out the words "other than" and "immediate".

[R–26] and change the words "671, 'Operating Rents'" to the words "[613], Amortization of intangible property".

[R–27] In present paragraph (D) of this instruction, insert at the end the words "When classes of outside plant are subdivided between exchange and toll or by areas, separate retirement unit costs shall be used to insure that exchange and toll plant and the plant of various areas will be accurately credited with the book cost of plant retired".

[R–28] In present paragraph (E) of this instruction, strike out the word "and" in line 2 and insert after "property" the words "and Telephone plant purchase adjustment"; strike out in lines

4, 5, and 6 the words "account 673, 'Telephone franchise requirements,'" and "675, 'Other expenses'", and insert after "account" in line 5 the words "[613], Amortization of intangible property", and "account [100.2], Telephone plant purchase adjustment".

[R-29] Insert a new instruction to follow present instruction 25 as follows:

[26]. Work order system required

(A) Companies shall record all changes in telephone plant used wholly or partly in telephone operations by means of a work order or job order system. Such work orders and supporting records shall be permanently preserved. The work order system shall include a Work Order Estimate and a Work in Progress Record, and shall contain the particulars described below.

(B) All installations, additions, retirements, or replacements shall be covered by a Work Order Estimate and a Work in Progress Record. Projects of less than $200 may be covered by standing work orders.

(C) The Work Order Estimate shall include the following particulars:

(1) A designation number or letter and the signature of the officer or employee who authorized the work or purchase. If authorization is by the board of directors or other body, the proper officer shall so state over his signature.

(2) A description and the location of the work to be done (or the purchase to be made), the dates between which such work (or purchase) is to be accomplished, the date when the work was begun, and the date when finished.

(3) Detailed estimates of the cost of the work, together with maps, plans, diagrams, specifications, etc., applicable.

(4) The account or accounts to which the cost of the project is chargeable and the amount chargeable to each account.

(5) Any variations between estimates and actual costs of the project.

(6) When a retirement, replacement, betterment, or rearrangement of property is involved, the Work Order Estimate shall show or refer to other records which cover the book cost (estimated if not known, and the basis of the estimate to be stated) and the date of installation of the property withdrawn, enlarged, rearranged, improved, or replaced, and the name and page of the accounting and engineering books and records covering such installation and the cost thereof. If a work order system was in use at the time such property was installed, reference thereto shall be made by number or other designation.

(D) The Work in Progress Record shall contain the following particulars:

(1) A designation number or letter which shall correspond to the number or letter on the Work Order Estimate covering the same project. When more than one such Work in Progress Record covers the work on a Work Order Estimate, each shall be numbered or lettered in such manner as to be readily identifiable with the Work Order Estimate for the same project.

(2) The accumulated charges applicable to each particular job or project separately for each of the items set forth in instruction 22B, and the total cost of the completed project. The cost of dismantling and the salvage realized shall be shown separately. When any project involves charges to more than one telephone plant account, a separate work in progress record shall be kept for the work chargeable to each account. Every charge or credit on work in progress records shall refer to the voucher, journal, or other source from which the entry therein was made.

(3) Full details at any time of the amount carried in account [100.1], "Construction work in progress." The cost of completed projects shall be promptly transferred from that account to the accounts to which chargeable.

Upon coming into service, completed portions involving additions to telephone plant accounts shall be transferred to the appropriate accounts although other portions of the work covered by the same work order are not yet completed and the work order has not been closed. Credits for such transfers shall be made in separate columns.

NOTE A.—Requirement of the use of the Work Order System here outlined may be suspended by order of the Commission in the case of a company which satisfies the Commission that the system which it has in use for recording changes in telephone plant accounts gives the equivalent detail by accounts in substantially the same form. The identification of expenditures with property must be complete and clear, and the detail of the cost of each project or job (see instruction 22B (1) to (11) must be readily available. The total of the uncompleted projects must also be in agreement with account [100.1] "Construction work in progress."

NOTE B.—The Work Order System is required to record changes in telephone plant accounts. Its use is recommended, however, in recording other expenditures, such as for fixed capital in other departments, maintenance work, etc. When used for maintenance work, balances applicable thereto shall be cleared monthly to the appropriate accounts.

[R–30] Insert a new instruction following the above instruction to read as follows:

[27] Telephone plant, perpetual inventory required.

(A) Not later than January 1, 1934, each company shall begin the preparation of a continuing or perpetual inventory of telephone plant subdivided geographically as required by any state commission having jurisdiction. The inventory shall be completed not later than January 1, 1935.

(B) The perpetual inventory shall be arranged in conformity with the telephone plant accounts prescribed in this classification and shall contain a description and classification of the property in such detail as may be required by the state commission having jurisdiction or, where there is no state commission having jurisdiction, by this commission.

[R–31] Instruction 31. Income from sinking and other funds.—In the next to the last line insert after "Provident reserve" the words "account 173, Employment stabilization reserve,".

[R–32] Instruction 64. In lines 7–8, change "maintenance" to "retirement".

[R–33] Instruction 70. Purpose of clearing accounts. Insert at the end of instruction but before parenthesis the words "unless a state commission having jurisdiction shall require otherwise".

[R–34] Instruction 80. Computation and filing of depreciation rates. In lines 3–4 of paragraph (A) strike out the words "for review and recommendations to this Commission"; after "property" in line 16 insert the words "Such percentage rates shall not include any allowance for the loss in service value of property expected to be installed in the future"; after the word "it" in the third line on page 21, insert the words "The state commission or commissions having jurisdiction shall fix the composite annual percentage rates of depreciation which shall be charged with respect

to each class of depreciable telephone plant and issue an order prescribing such rates. Where no state commission has jurisdiction or is willing to act in the premises, such rates shall be fixed and an order issued by this commission." Strike out the next sentence in lines 3–7 on page 21; in line 8 change "after" to "before" and "the temporary order" to "such orders"; in lines 10–11 strike out "with a view to the modification of such order"; in line 12 insert after "conducted" the words "by the state commissions with respect to orders issued by them, and, so far as possible, for this commission with respect to such orders as it may issue"; and strike out the balance of this sentence in lines 12–13; in line 14 insert after the word "Commission" the words "or by the state commission having jurisdiction".

In paragraph (B) of this instruction at the end of the first line, insert the words "a state commission or by".

[R–35] *Instruction 81. Depreciation charges.* In paragraph (A) strike out all of line 3 except the word "and" and insert "to clearing accounts,".

[R–36] In paragraph (C) insert after "prescribed" in line 4 the words "by the state commission having jurisdiction or"; put a period after "Commission" at the end of line 4; strike out "except that" and "previously" in line 5 and "by this commission" in line 6; in lines 2 and 3 on page 22 strike out everything after "used".

[R–37] *Instruction 82. Classes of depreciable telephone plant.* Insert a note to read as follows:

NOTE.—When depreciable plant carried in account 276, "Telephone plant purchased", is distributed to the appropriate plant accounts, adjusting entries shall be made covering the depreciation charges applicable to such plant for the period during which it was carried in account 276, "Telephone plant purchased."

[R–38] *Instruction 83. Plant retired for causes not factors in depreciation.* In line 8 insert after "approval of" the words "any state commission having jurisdiction and"; change "Extraordinary maintenance suspense" to "Extraordinary retirement suspense" and in line 12 after "as" insert the words "the aforesaid state commissions and".

[R–39] *Balance sheet statement.* Insert after account 100, Telephone plant, an account entitled "[100.1], Construction work in progress", and an account entitled "[100.2], Telephone plant purchase adjustment". Insert a new account to follow account 101, entitled "[101.1], Advances to affiliated companies." Insert two accounts to follow account 118, entitled "[118.1], Notes receivable from affiliated companies" and "[118.2], Accounts receivable from affiliated companies." Insert a new account to follow account 122,

entitled "[122.1], Subscriptions to capital stock." Insert a new account to follow account 134, entitled "[134.1], Capital stock expense". Change title of account 138 to read "Extraordinary retirement suspense." Insert after account 152 a new account, entitled "[152.1], Capital stock subscribed", and change the title of account 153 to read "Installments paid on capital stock". Insert after account 159, two new accounts entitled "[159.1] Notes payable to affiliated companies" and "[159.2] Accounts payable to affiliated companies." Change title of account 175 to read "Contributions for extensions."

[R-40] *Account 100. Telephone plant.* Insert in line 1 before "company's" the words "cost of the" and strike out the words "investment in" in line 2.

[R-41] Transfer account "[100.1] Construction work in progress", on pages 50–51 to follow account 100, "Telephone plant". Revisions to text of this account are made under its present position.

[R-42] Create a new balance sheet account as follows:

Account [100.2] Telephone plant purchase adjustment.

(A) This account shall include the difference between (*a*) the cost to the accounting company of telephone plant purchased; and (*b*) the actual original cost of construction and installation of such plant, of the governmental franchises and similar rights acquired, and of land acquired, less the amount or amounts credited to the depreciation and amortization reserves and to account [175], "contributions for extensions". If the actual original cost is not known, the entries in this account shall be based upon an estimate of such costs. (See also instruction 21.)

(B) This account may be subdivided according to the character of the amounts contained therein.

(C) The amounts recorded in this account with respect to each property purchase shall be disposed of, written off, or provision shall be made for the amortization thereof in such manner as the commission having jurisdiction may direct. (See instruction 21.)

[R-43] *Account 101. Investments in affiliated companies.*—In paragraph (A) strike out the word "book" in line 2; change the parenthesis to read "(except as provided in instruction 12–B)";

[R-44] and strike out the last two lines, putting a period after "investments" in line 5.

[R-45] In paragraph (B) change items to read "(1) Common stocks, (2) Preferred stocks, (3) Funded debt."

[R-46] In paragraph (C) strike out Note [s]A

[R-47] and [strike Note]B.

[R-48] Create a new account to follow account 101, as follows:

[101.1], Advances to affiliated companies.

This account shall include the amount of the investment advances to affiliated companies. (See instruction 3–M.)

NOTE.—Amounts receivable from affiliated companies which are subject to current settlement shall be included in accounts [118.1] or [118.2].

[R–49] [Additional] *Account 102. Other investments.* (A) In second line strike out the word "book" and change the parenthetical phrase to read as follows: "(Except as provided in instruction 12–B)."

[R–50] *Account 103. Miscellaneous physical property.*—In lines 3–4 change "account 100" to read "accounts 100, [100.1] and [100.2]"; at the end of line 5 after "service" insert "within one year"; and strike out the words "and held other than for immediate sale" in lines 7–8; also strike out the note.

[R–51] *Account 116. Temporary cash investments.*—Strike out the word "book" in line 2 and insert after the word "cost" in line 2, "(See also instructions 11 and 12)". Omit parenthetical clause from line 6. Add the words "Do not include herein any securities of affiliated companies."

[R–52] *Account 117. Notes receivable.*—Strike out the word "book" in line 1 and move the parenthesis to follow "cost" in line 2; and change the note by striking out "and" in line 3, inserting after "advances" the words "and notes issued by affiliated companies", and by striking out "or" in line 4 and inserting at the end, "or [118.1]."

[R–53] Insert before account 120 two new accounts to read as follows:

[118.1], Notes receivable from affiliated companies.

This account shall include demand or time notes, bills and drafts receivable, or other similar evidences (except interest coupons) of money receivable from affiliated companies within a time not exceeding one year from date of issue.

NOTE A.—This does not include obligations any part of which matures more than one year from date of issue.

NOTE B.—Exclude from this account notes that are within the definition of account 101, "Investments in affiliated companies", or account [101.1], "Advances to affiliated companies."

[R–54] [As amended] "[118.2], Accounts receivable from affiliated companies.

This account shall include amounts due from affiliated companies on all transactions that are subject to current settlement, except for sales of telephone service at regular rates. There shall be included accounts receivable arising from divisions of toll revenues.

Note. If terms included in this account are not actually paid currently they shall be transferred to account [101.1], "Advances to affiliated companies."

[R–55] Add to *Account 120, "Accounts receivable"*, a note reading as follows: "NOTE.—Exclude from this account accounts receivable from affiliated companies".

[R–56] *Account 122. Material and supplies.*—In line 4 of paragraph (A) change the word "articles" to the words "materials and articles owned by the company".

[R–57] After account 122 insert a new account to read as follows:

[122.1] Subscriptions to capital stock.

This account shall include the balance owing from subscribers upon legally enforceable subscriptions to capital stock. It shall be debited with the agreed purchase price. Concurrently credits shall be made to account [152.1], "Capital stock subscribed." Payments received from subscribers shall be credited to this account.

NOTE.—The records supporting the entries to this account shall be kept so that the corporation can furnish the name and address of each subscriber, the amount and kind of capital stock subscribed, the date of subscription, the date that each payment is due and the date that each is paid, the nature of each payment (whether cash or other consideration), and any other information that is necessary to make the history of the subscription complete.

[R–58] Insert a new account following *Account 134, "Discount on capital stock,"* as follows:

"[134.1], Capital stock expense.

(A) This account shall include all expenses in connection with the issuance and sale of capital stock.

(B) When any issue of capital stock, or a portion thereof, has been superseded or cancelled, there shall be credited to this account and charged to account 413, "Miscellaneous debits to surplus", the amount of all charges herein in respect of such superseded or cancelled stock.

(C) The company may amortize the balance carried in this account by credits hereto and concurrent charges to account 323, "Miscellaneous income charges", or account 413, "Miscellaneous debits to surplus."

Items (Note instruction 8)

Fees and commissions paid, including cash value of securities issued, to promoters, underwriters, brokers, or salesmen.

Fees and expenses in obtaining permission from regulatory bodies for the issuance of stock and in filing papers of notification thereunder.

Fees and taxes for the issuance of capital stock.

Listing capital stock on exchanges,

Preparing, engraving, printing, issuing and distributing prospectuses and certificates in connection with original and additional stock issues.

Revenue stamps on new issues of capital stock.

Soliciting subscriptions for stock, including fees, commissions and advertising.

NOTE.—Exclude herefrom and include in account 413, "Miscellaneous debits to surplus," expenses in connection with the reacquisition and resale of stock.

[R–59] *Account 138, Extraordinary maintenance suspense.* Change title to "Extraordinary retirement suspense". In paragraph (C) insert after "permission of" the words "any state commission having jurisdiction and of"; strike out the words "to this Commission" in the last line on page 30.

[R–60] *Account 139, Other deferred debits.* In line 10 insert after "preliminary" the word "engineering,"; put a period instead of a semicolon after "sold" in line 18; strike out "other" in line 18.

[R–61] *Account 150, Capital stock.* In paragraph (A)(1)(c) add at the end the words " with the approval of the state commission having jurisdiction ".

[R–62] Strike out the present account 153, Capital stock installments, and substitute in place of it two accounts as follows:

[152.1], Capital stock subscribed. This account shall include the agreed purchase price of stock for which legally enforceable subscriptions have been received, but for which at the date of the balance sheet certificates have not been issued. A separate subdivision shall be maintained for each class of stock. Credits to this account shall reflect the agreed purchase price (exclusive of accrued dividends, if any) of the stock and shall be so recorded as to show separately in respect of stock with par value, the par amount of stock subscribed for and the discount or premium thereon. This account shall be debited when a subscriber has paid his subscription in full and stock certificates are issued representing the shares subscribed.

[153], Installments paid on capital stock. This account shall include the amount of installments paid on capital stock on a partial or installment payment plan by subscribers against whom there is no legally enforceable subscription contract, and who are entitled to be reimbursed for the principal amount of their payments, with or without interest, in case they fail to complete payments for the stock and receive certificates therefor.

NOTE.—The record supporting the entries to this account shall be kept so that the corporation can furnish the name and address of each subscriber, the amount and kind of capital stock subscribed, the date of subscription, the date that each payment is due and the date that each is paid, the nature of each payment (whether cash or other consideration), and any other information that is necessary to make the history of the subscription complete.

[R–63] *Account 156, Advances from affiliated companies.* In the note change " account " on line 2 to " accounts [159.1] or [159.2] ". Strike out balance of line.

[R–64] *Account 158, Notes payable.* Insert in line 2 after " indebtedness " the words " to nonaffiliated companies or individuals."

[R–65] *Account 159, Accounts payable.* Insert in line 2 of paragraph (A) after " others " the words " (except affiliated companies)."

[R–66] *After Account 159, Accounts payable,* insert two new accounts as follows:

[159.1], Notes payable to affiliated companies. This account shall include the face value of notes, drafts, acceptances, or other similar evidences of indebtedness payable on demand or within a time not exceeding one year from the date of issue, to affiliated companies.

NOTE A.—Exclude from this account notes that are within the definition of account 156, "Advances from affiliated companies."

NOTE B.—The record supporting the entries to this account shall be so kept that the utility can furnish complete details as to each note, when it was issued, the consideration received, and when it is payable."

[R–67] [As amended] [159.2], Accounts payable to affiliated companies. This account shall include amounts owed by the accounting company to affil-

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iated companies on all transactions subject to current settlement except for purchases of telephone service at regular rates. There shall be included accounts payable arising from divisions of toll revenues.

NOTE.—If items included in this account are not actually paid currently, they shall be transferred to account 156, "Advance from affiliated companies."

[R–68] *Account 160, Customers' deposits.* Insert an additional note to read as follows:

NOTE B.—Unclaimed customers' deposits shall be carried in this account until (*a*) other disposition of them is authorized by the state commission having jurisdiction or this Commission, or (*b*) they may be transferred to the State by statute.

[R–69] *Account 170, Provident reserve.* In line 2 of paragraph (B) change "Relief and pensions" to "Employees' pensions and benefits."

[R–70] *Account 171, Depreciation reserve.* In paragraph (A) change "Account 702, Vehicle and other work equipment expense" to "clearing accounts".

[R–71] In paragraph (B) change "maintenance" to "retirement."

[R–72] *Account 172, Amortization reserve.* Change paragraph (A) to read as follows:

(A) this account shall be credited with amounts concurrently charged to account [613], 'Amortization of intangible property', for the amortization of franchises, patents, leaseholds, etc." (See also instruction 25–E.)"

[R–73] In paragraph (C), line 5 on page 37, strike out the words "the appropriate surplus account" and insert in their place "account [613], 'Amortization of intangible property'."

[R–74] *Account 173, Employment stabilization reserve.* Strike out this account. If this is not done, add the following note: "NOTE.—This account shall be used only with the approval of both this Commission and the State commission having jurisdiction."

In paragraph (B) change "Relief and pensions" to "Employees' pensions and benefits."

[R–75] *Account 175, Donations.* Strike out all of this account except the number, and substitute the following:

Contributions for extensions.

(A) this account shall include contributions to the company by subscribers, governmental bodies, or organizations, of labor, property, or money made for the purpose of establishing, extending, or improving the service rendered by the company, when such contributions are not subject to refund. The records shall be kept so that the amount and description of each contribution, together with the location and description of property to which it relates, will be readily available.

(B) No debits shall be made to this account except when there is permanently discontinued by the company the service in connection with which the contribution was made, because of sale of that portion of the business or otherwise.

NOTE A.—Advances or conditional contributions which are subject to refund shall not be credited to this account but to account 174, "Other deferred credits." Donations to cover current operating expenses or deficits shall be credited to account 402, "Miscellaneous credits to surplus".

NOTE B.—When the contribution consists of property, it shall be charged to the telephone plant accounts at its original cost new (estimated, if not known) and there shall be credited to the depreciation reserve and amortization reserve accounts the estimated amount of accrued depreciation and amortization computed in accordance with instruction 80 and account 172, respectively, with due consideration of the age of the property. The difference between the amounts so includable in the telephone plant and the reserve accounts shall be credited to this account.

[R–76] List of telephone-plant accounts. Strike out account 280, "Construction work in progress."

[R–77] *Account 201, Organization.* Strike out the words "and the expense of issuing capital stock"; also strike out items 3, 4, 5, 7, 8, and 9.

[R–78] and strike out the words "and preparing" and "for operation" in item 6.

[R–79]Strike out the parenthetical clause at end of text and insert in its place "(See also account [134.1], 'Capital stock expense')".

[R–80] Strike out the notes and substitute for them the following:

NOTE A.—This account shall not include any discounts upon securities issued, nor shall it include any costs incident to negotiating loans, selling bonds or other evidences of debt, or expenses in connection with the authorization, issuance, or sale of capital stock. (See instruction [14] and account [134.1], "Capital stock expense.")

NOTE B.—Exclude from this account, and include in account 664, "Law department", the cost of repairing and filing papers in connection with the extension of the term of incorporation unless the first organization costs have been written off.

NOTE C.—When charges are made to this account for expenses incurred in mergers, consolidations or reorganizations, amounts previously included herein on the books of the various companies concerned shall not be carried over.

[R–81] *Account 211. Land.* In paragraph (A) change "held" in line 3 to "used", and strike out the balance of the first sentence after the words "right of way" in line 5.

[R–82] *Account 212. Buildings.* In paragraph (B) insert after the word "service" in line 2 the words "within one year".

[R–83] *Account 276. Telephone plant purchased.* Change "may" to "shall"; insert after "cost" the words "to the company" and insert at the end of the text "and to other accounts". Strike out note A.

[R–84] *Account 277. Telephone plant sold.* Strike out note A.

[R–85] *Account 278. Undistributed cost of property.* Insert at the end of line 3 after "accounts" the words "or to account" [100.2], "Telephone plant purchase adjustment"; strike out the rest of the text except the parenthesis. Insert in the note after the word "insurance", the words "employees' pensions and benefits,"; insert a new note to read as follows:

NOTE B.—Before any charge is made to this account there shall be submitted to any state commission having jurisdiction and to this Commission a complete statement of the reasons for the entry, together with a copy of the proposed entry.

[R–86] *Account 280. Construction work in progress.* Transfer this account to follow account 100 on the balance sheet. Also insert after the word "service" in line 5 of paragraph (A) the words "within one year from the date of its acquisition"; and insert at the end of paragraph (B) the words "in no case shall any amount be carried in this account at the end of any month for plant which is actually in service." Strike out note B.

[R–87] *Account* 303. Rent for lease of operating property. Change "account 702" in line 2 of Note C to read "clearing accounts".

[R–88] *Account 313. Interest income.* Strike out the last sentence in paragraph (A) and insert in its place the words "(see account 526)".

[R–89] *Account 323. Miscellaneous income charges.* Change the second item in the list to read as follows "Membership fees and dues in associations, other than those of the company itself in associations of telephone companies and of employees in professional organizations".

[R–90] *Account 402. Miscellaneous credits to surplus.* Strike out the last two items on page 59.

[R–91] *Account 413. Miscellaneous debits to surplus.* Change the tenth item to read as follows: "Donations or contributions, including those made for charitable or social or community welfare purposes. (See also account 672, 'Employees' pensions and benefits'.)"

[R–92] Insert a new item as follows: "Losses of funds due to bank failures".

Insert "of" in item 14.

[R–93] *Account 526. Other operating revenues.* Strike out "and" from next to last line and after the word "operations" add "; and interest on funds used in telephone operations."

[R–94] Operating expense accounts. Change the list of maintenance expense accounts for class A companies to read as follows:

I. Maintenance expenses.
[601] Supervision of maintenance.
[602a] Repairs of pole lines.
[602b] Repairs of aerial wire.
[602c] Repairs of aerial cable.
[602d] Repairs of underground conduit.
[602e] Repairs of underground cable.
[602f] Repairs of submarine cable.
[604] Repairs of central office equipment.
[605] Repairs of station equipment.
[606] Repairs of buildings and grounds.
[607] Station removals and changes.
[610] Maintaining transmission power.
[611] Employment stabilization.
[612] Other maintenance expenses.

Detailed texts for those maintenance accounts have not been prepared.

[R–95] Create a new subdivision of operating expense accounts for both class A and class B companies, to read as follows:

II. Depreciation and amortization.
608 Depreciation.
609 Extraordinary retirements.
[613] Amortization of intangible property.

[R–96] Change the title of account 672, "Relief and pensions," to "Employees' pensions and benefits".

[R–97] *Account 605. Repairs of station equipment.* Change "maintenance" at end of paragraph (B) to "retirement".

[R–98] *Account 608, Depreciation.* In lines 3–4 strike out everything after "except" and substitute "amounts chargeable to clearing accounts."

[R–99] *Account 609. Extraordinary retirements.* In line 3, change the word "maintenance" to "retirement"; in line 4, insert after "authority of", the words "any state commission having jurisdiction and of".

[R–100] Insert in the depreciation and amortization group a new account to read as follows:

[613] Amortization of intangible property.

(A) This account shall be charged each month with the amount necessary to cover such portions of the lives of limited term franchises, patents, leaseholds, and similar intangible property included in the telephone plant accounts, as have expired during the month. Amounts so charged shall be credited to account 172, "Amortization reserve."

(B) This account shall also be charged or credited with the loss or profit at the retirement of any item of intangible property listed above, as provided in account 172, "Amortization reserve."

[R–101] *Account 611. Employment stabilization.* Strike out this account. If this is not done, insert in line 6 after the words "ap-

proval by" the word "both" and after "commission" the words "and the state commission having jurisdiction".

[R–102] *Account 661. Executive department.* Strike out the fifth item under "Expenses and supplies" and also the note. In accounts 662, 663, and 664, strike out the same item and the same note as in 661.

[R–103] *Account 663. Treasury department.* In note B, second line, change "201" to "[134.1], 'Capital stock expense'".

[R–104] [As amended] *Account 664. Law department.* In the eleventh item under "Expenses and supplies", strike out the words "rate cases or". Add at end of note B "(See also account [670], 'Regulatory commission expenses')".

[R–105] Insert a new account as follows:

670. Regulatory commission expenses.

(A) This account shall include expenses incurred by the company in connection with formal cases before federal or state regulatory commissions, or in cases in which such a commission is a party, other than those expenses includible in account 202, "Franchises," account [134.1], "Capital stock expense," or account 135, "Discount on funded debt." It shall also include costs incurred by regulatory commissions which are collected from the company.

(B) This includes such items as:

1. Fees, retainers, and expenses of counsel solicitors, attorneys, accountants, engineers, clerks, attendants, witnesses, and others whose services are devoted to the defense or prosecution of petitions or complaints presented to federal or state regulatory commissions.

2. The pay of officers and employees specially assigned to or engaged in the valuation of property owned or used by the company in connection with such cases; also the cost of similar work performed by others.

3. Office and traveling expenses, stationery, printing, engineering supplies, and other expenses and supplies including expenses of officers and employees upon matters covered by this account even though no portion of their pay is assignable thereto.

NOTE.—Expenses incurred for the improvement of service, additional inspection, or in rendering reports, which are made necessary by the rules and regulations, or orders, of federal or state regulatory commissions, shall be charged to the appropriate operating expense accounts.

[R–106] *Account 671. Operating rents.* Strike out paragraph (C).

[R–107] *Account 672. Relief and Pensions.* Change title to "Employees' pensions and benefits." In paragraph (D), insert after the word "inform" in the second line, the words "any state commission having jurisdiction and". Strike out paragraph (F); if this is not done insert the words "any state commission having jurisdiction and" after "approval by" in the sixth line. Insert a new paragraph to read as follows:

(G). There shall be credited to this account that portion of each class of Employees' pensions or benefits attributable to construction, plant removal, and custom work labor.

[R–108] *Account 673. Telephone franchise requirements.* Strike out paragraph (B).

[R–109] [As amended] *Account 675. Other expenses.* Strike out paragraph (B). Strike out the words "Amortization of patents" and "or in an undeveloped state and patents of doubtful service value" in the first item;

[R–110] [Strike] the entire fourth item;

[R–111] and [Strike] the entire last item.

[R–112] Insert a new item as follows:

Membership fees and dues, of the company itself in associations of telephone companies, and of employees in professional organizations.

[R–113] Strike out note (D).

[R–114] [As amended] Change parenthetical clause at end of note C to read "(See also account 670 and instruction 63)". Change sixth item to read "Cost of valuations, inventories, and appraisals of telephone plant, taken in compliance with orders of Federal, State, or other regulatory authorities not chargeable to account 670, "Regulatory commission expense". (See also notes B and C to this account.)

[R–115] *Account 702. Vehicle and other work equipment expense.* Insert a semicolon after the word "stables" in line 4, and add at the end of paragraph (A) ", except equipment of store rooms".

[R–116] *Account 704. Supply expense.* Add at the end of paragraph (A) "; and the amount of depreciation charges applicable to the accounting period for equipment of store rooms".

[R–117] *Account 705. Engineering expense.* Revise paragraph (B) to read as follows:

(B) This account shall be cleared by charges to the appropriate accounts on the basis of service rendered, as determined by the time and expense devoted to particular jobs.

Insert a new paragraph as follows:

(C) If projects, on which expenses included herein are incurred, are not carried out, the amount of such expenses charged thereto shall be charged to account 413, "Miscellaneous debits to surplus." (See also account 139, "Other deferred debits".)

[R–118] *Account 706. Plant supervision expense.* In paragraph (B) strike out the words "apportioning such expense" and insert the word "charges" instead. On page 92 insert after "time" the words "and expense" and strike out everything after "jobs", inserting instead the words "unless another basis is required by order of the state commission having jurisdiction". In the note in line 3 strike out "work" and substitute the words "and plant removals".

Comments were made with respect to portions of the foregoing by representatives of the 21 commissions and counsel for the tele-

phone companies, and the several recommendations were discussed in detail by the comptroller and assistant comptroller of the American Telephone and Telegraph Company, hereinafter referred to as the American Company.' The independent companies adopted the comment of the representatives of the Bell system companies.

The latter companies, while indicating that they are not entirely satisfied with the uniform system, offered no amendments thereto. They are, moreover, in favor of retaining it in its present form rather than modifying it in line with any of the suggestions or recommendations of the State commissions.

Inasmuch as the Bell system companies have put the system into effect as of January 1, 1933, they are, of course, opposed to its being rescinded. The independent companies state that they are satisfied with the uniform system as it stands and they emphasize the importance of simplicity. All the telephone companies stress the desirability, importance, and indeed the necessity of uniformity in accounting.

As a preliminary to the discussion of the recommendations, which will be treated in the order above stated, attention should be directed to the fact that many of them involve delegation or surrender of authority granted to us. Some are in conflict with the decision in the *Depreciation case.* With respect to others, the proper result can preferably be reached by the introduction of schedules calling for the segregation of pertinent accounting data in our forms for annual reports of telephone companies. Changes in such schedules may be readily made from time to time without modifying the uniform system. Any impairment of the usefulness of the latter for the administrative purposes of the telephone companies is, of course, to be avoided.

(R–1) This is a proposal to amend the fifth ordering clause of the order of November 12, 1932, herein, so as to make mandatory the subdivision of accounts in the manner ordered by any State commission having jurisdiction. In support thereof the 10 commissions assert that, whereas under instruction 2, "Records", (C) (1), the companies may for their own purposes subdivide any of the accounts prescribed, the permission granted by the fifth ordering clause, to subdivide to the extent necessary to secure the information required in the prescribed reports to commissions having jurisdiction, may be subject to a too narrow construction.

It was our thought that the authority of the State commission would suffice to require the desired subdivision, provided permission for such subdivision is granted in the uniform system. The State commissions apparently fear that their own authority would not be

sufficient for this purpose, even if such permission be granted, and therefore ask us to fortify their authority by exercise of our own. There appears to be no sufficient reason why this should not be done, and we therefore find that the clause in question should be amended to read as follows:

It is further ordered, That any such carrier or receiver or operating trustee of any such carrier, shall subdivide the accounts hereby prescribed in the manner ordered by any State commission having jurisdiction or to the extent necessary to secure the information required in the prescribed reports to such commission: Provided, however, that in no event shall the integrity of any primary account be impaired.

(R–2) This would amend instruction 2, "Records", (C) (2), by providing that clearing accounts in addition to those prescribed may be kept in response to requirements imposed by State commissions having jurisdiction.

It is an underlying principle of the uniform system that items which are directly assignable to the several primary accounts should be so charged. Recognizing that not all of the costs incurred are thus assignable, we have prescribed clearing accounts in those cases where the necessity therefor was anticipated, in order to facilitate distribution of items to the proper accounts. It is further provided by the instruction in question that additional clearing accounts may be kept when necessary to make such distribution.

It follows that the field has been covered and that the amendment in question is unnecessary.

(R–3) This involves the amendment of instruction 2, "Records", (C) (3), so as to provide that, in addition to the accounts prescribed, temporary or experimental accounts may be kept in obedience to the requirements of a State commission having jurisdiction.

In its present form the scope of this instruction is confined to accounts for the purpose of developing the efficiency of operations, etc. Within that field the State commissions are, of course, free to exercise whatever authority they possess with respect to requiring temporary or experimental accounting. Under the proposed revision, however, no limitation is imposed short of the entire field of accounting. The statement of the proposition carries the conviction that it is unduly broad. If adopted, moreover, the question as to what constitutes temporary or experimental accounting would have a tendency to assume paramount importance.

We are unable to see wherein this revision is warranted.

(R–4) This would add to instruction 2, "Records", a new paragraph, (E), providing that the forms of statements, for balance-sheet accounts and the various other groups except clearing accounts, shall not be construed as preventing any State commission having

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jurisdiction from requiring the use of different forms for, or the subdivision of accounts in, such statements in reports to it.

The proposal is ambiguous in that it may apply to mere abstracts and analyses of accounting performed in pursuance of the uniform system, or to the text of the several accounts prescribed thereby and their classification thereunder. If the former is intended, the proposed revision is unnecessary, as the matter is clearly not within the purview of the uniform system. On the other hand, if the latter is intended, the proposal involves the surrender of power to prescribe the manner in which the accounts shall be kept and would endanger the integrity of the accounting we have prescribed.

The matter of subdivision of accounts has been covered by our comment under R–1.

(R–5) This would add, following instruction 2, "Records", a new instruction [2.1 "Submission of journal entries, etc.,"] to the effect that certain matters, which under the provisions of the uniform system are to be submitted to us for approval or decision, shall first be submitted to the State commission having jurisdiction; that the decision of the latter shall be forwarded to us by the company with a statement indicating its acceptance or rejection thereof, and in the event of the latter, pointing out wherein the decision is deemed to conflict with the uniform system; and that a copy of such statement shall be filed with the State commission.

Aside from questions involving matter of form and the probability that the adoption of such procedure would entail undue delays, we think that the proposal is otherwise objectionable. We strongly favor cooperation with State commissions, and believe that they should have notice of the pendency of matters of the kind under discussion and an opportunity to present their views, and that they should be advised of our decisions thereon. However, it seems neither necessary nor appropriate to incorporate the procedure for such cooperation in the uniform system. The proposed revision must accordingly be rejected.

(R–6) This involves the amendment of subparagraph (a) of instruction 3, "Definitions", (D), to include among the conditions to be considered as constituting forms of control, the following:

(6) Ability to control the action of the company with or without the major part of the voting power in the controlled company.

An examination discloses that such a provision would be redundant, because subparagraph (a) defines "control" as meaning the ability to determine the action of a company.

(R–7) Proposes the amendment of instructions 3, "Definitions" (E), by adding the words shown in italics, so as to read as follows:

"Book cost" means the *gross* amount at which property is recorded in these accounts *without deduction of related reserves.*

The principle underlying the investment accounts is that they shall record the cost of property to the accounting company. While a consideration of the related reserves might be relevant to the *value* of property, they do not enter into the *cost* thereof.

The uniform system, of course, contemplates decreases in book cost from that initially recorded, as a result of partial retirements in the case of physical property, writing down in the case of securities, and other proper adjustments. Hence, the use of the term "gross", which may have been inserted merely for the purpose of antithesis, might prove to be misleading.

We do not think that the recommendation is conducive to a better understanding of the meaning intended.

(R–8) Proposes to add to instruction 3, (J), which defines depreciation in accordance with the order in the *Depreciation case*, a statement enumerating some of the items included in the causes to which reference is made in said definition.

The recommendation should not be adopted in its present form, because with respect to the items enumerated it would be susceptible of being construed as dispensing with the qualifications attached to the word "causes" in the present definition. In the *Depreciation case*, considerable attention was given to the matter of defining depreciation, and we deem it preferable to leave the question of what is included in the causes thereof to be determined in accordance with the facts in each case.

(R–9) This would insert in instruction 3, "Definitions", following paragraph (S) a definition of "original cost." It is in substantial accord with the definition heretofore accepted by us. *Montour R. Co.*, 33 Val. Rep. 681, 682. The continuity would be improved by a slight modification of the parenthetical phrase and a transposition of the word "of". The last clause, while essentially surplusage, may emphasize and clarify the intent.

The proposed definition should be adopted, with the modifications indicated, as follows:

(S.1) "Original cost" means the actual money cost of (or the current money value of any consideration other than money exchanged for) property at the time when it was first devoted to the public service, whether by the accounting company or by a predecessor public utility.

It follows that the term "book cost" should be substituted for "original cost" in the following portions of the text of the uniform system where the latter term in the sense above defined is not intended:

Page 28, Account 122 "Material and supplies" (D), line 2 of subparagraph (2);

Page 70, Account 607 "Station removals and changes", line 2 of paragraph (B).

(R–10) This would amend instruction 3, "Definitions", (V), by eliminating the words "and recovery" following the word "removal" so as to read as follows:

"Replacing" and "replacement", when not otherwise indicated in the context, mean the construction or installation of telephone plant in place of plant retired together with the removal of the plant retired.

The reason assigned for this proposal is that the definition in its present form tends to confuse with the cost of removal "items of expense which, if incurred, are to be deducted in arriving at gross salvage." This statement is somewhat obscure. We are not advised of any advantage to be gained by requiring a separation between the cost of removal and the cost of recovery up to the point where the material is in the store-room or available for sale. Moreover, from the standpoint of field operations such a separation appears to be impractical. On the other hand, if the statement refers to those incidental costs connected with the sale of recovered material, such as advertising, crating, etc., there is no occasion for confusion, because these items are includible in account 704 "Supply expense".

(R–11) Proposes amending instruction 3, "Definitions", (BB), by adding the words shown in italics so as to read as follows:

"Telephone plant" means physical property used in telephone service and physical property held for such service under a definite plan *for its use within one year from date of acquisition.*

The present definition of telephone plant is intended to cover all physical property which is either actually used as such by the owner or others, or definitely held for such use. All other physical property is defined as miscellaneous physical property. This separation recognizes the principle that physical property may be characterized as telephone plant, not only by its actual use in that capacity, but by its intended use therein.

It will be noted that the proposed revision recognizes the same principle, although it requires a definite plan for use in telephone service *within one year* as a prerequisite to classification as telephone plant. Apparently one of the important objects thereof is to bring the classification for accounting purposes into harmony with the requirements of valuation and rate investigations. It is doubtful, however, that such an arbitrary rule could be applied even in those cases. At any rate, where property is actually held for telephone service, it is clear that the exigencies of accounting preclude the drawing of a line of demarcation as sharp as might be drawn by a consideration of the facts in a particular valuation or rate investi-

gation. Furthermore, the provision that the cost of construction of telephone plant not completed ready for service shall be included in account 280 "Construction work in progress", facilitates a separation of telephone plant on the basis of actual use.

The proposed revision is rejected.

(R–12) Paragraph (C) of instruction 14, "Discount and premium on capital stock", requires that there be charged to the particular discount and premium account an amount equal to such portion of any credit balance therein as the company may elect to distribute to its stockholders, provided such distribution is permitted. The recommendation would restrict the operation of this provision to cases where distribution is permitted *by the State commission.*

We are not empowered to confer such authority upon a State commission. Where it possesses such authority, the proposed limitation would serve no purpose. In other instances, it would have no legal basis.

(R–13) This involves the amendment of paragraph (A) of instruction 20 "Purpose of telephone plant accounts", presumably in anticipation of the adoption of recommendations R–15 and R–16, so as to provide that the accounts mentioned are designed to show the *original* cost of the company's telephone plant.

Cost to the accounting company is the fundamental basis prescribed for charges to the plant accounts, and if the latter are kept in accordance with the uniform system, the balances shown for plant constructed by the company will approximate the original cost thereof to date. Moreover, as indicated by our comments under R–16 and R–15, respectively, the basis of charges for plant purchased is essentially cost to the accounting company, whereas with respect to plant donated, a basis is adopted which, in view of the nature of the transaction and the demands of uniformity in accounting, may properly be said to constitute an equivalent measure.

It does not, however, necessarily follow that there is any such relation of equivalence between the basis of charges prescribed for the two classes of plant last mentioned and the original cost thereof as defined under R–9. Indeed, the probabilities are that no such relation would exist. Accordingly, the recommendation is disapproved.

(R–14) This revision is proposed in order to coordinate paragraph (A) of instruction 20 "Purpose of telephone plant accounts" with the proposed definition of "telephone plant", which we rejected under R–11.

(R–15) This is a recommendation to eliminate paragraph (C) of instruction 20 "Purpose of telephone plant accounts," which provides

that telephone plant donated shall be charged to the plant accounts at its estimated current cost new with concurrent credits to reserve accounts to cover the estimated requirements for depreciation and amortization. The reference to the above paragraph made in paragraph (B) of the same instruction would also be eliminated.

It is proposed under recommendation R–75 to include as note B to account 175, "Contributions for extensions," [Donations] a substantially similar instruction except that original cost is made the basis instead of current cost new. So far as the matter of form is concerned, we perceive no advantage in the transposition. On the contrary, the instruction being of a general nature and dealing with several accounts, we think it is more in harmony with the scheme of the uniform system to include it in its present position.

With respect to the matter of substance presented, it would seem that from an accounting standpoint the logical manner of recording the acquisition of donated property would be to charge it to the appropriate accounts at its value as of the time of donation. In measuring such value we think that as between original cost and current cost new (less depreciation in both instances) the presumption is in favor of the latter as the better approximation.

(R–16) This recommendation was the subject of considerable discussion at the hearing. In substance it is as follows:

(1) In all cases of the purchase of property in use in telephone service, to require accounting for the purchase price through account 276 "Telephone plant purchased."

(2) To include such property in the primary plant accounts on the basis of original cost, estimated if not known.

(3) To set up in account 175 "Contributions for extensions" [Donations] the amount applicable to the property purchased that was recorded therein by the vendor.

(4) To include in a separate balance-sheet account, [100.2] "Telephone plant purchase adjustment," the amount necessary to adjust between the purchase price and the net of the charges to the primary plant accounts and the credits for depreciation and amortization requirements and donations.

These points will be treated in the above order.

(1) The uniform system provides that the cost of telephone plant purchased may be charged temporarily to account 276, pending distribution to the primary plant accounts. This procedure was adopted in recognition of the fact that the more desirable course of making the distribution directly cannot always be followed. Under the recommendation, the cost of plant purchased would invariably be charged to account 276, even though it were susceptible of being cleared therefrom immediately. The latter would thus constitute

what is sometimes called a memorandum account. However, we see no particular advantage to be thus gained, because the cost of telephone plant purchased would ordinarily be recorded as a single item which could be readily located.

(2) It appears from the record that the chief concern of the State commissions as to whether the accounting for telephone plant purchased should be on the basis of original cost or current cost new is related to the distribution of the proper amounts to the primary plant accounts for depreciation and amortization purposes.

Both the effective and the proposed provisions prescribe the same basis for items includible in account 202, "Franchises", and as a practical matter for "Construction work in progress." With respect to other items, it is clear that original cost as defined under R–9 is not necessarily the same as original cost to the accounting company, and, further, that it is precisely because the latter only is subject to the influence of prices current at the date of purchase, that the former basis is preferred by the State commissions. It should be remarked in passing that the undiminished original cost of "Station installations" and "Drop and block wires" should not be charged to the plant accounts in any event. For the sake of simplicity in accounting, such property is not treated as depreciable and therefore no reserve would be set up with respect thereto. It is for this reason that the uniform system provides that the charges to these accounts shall be based upon the estimated current cost new diminished in proportion to the expired service life.

The purchase price, of course, represents the cost to the accounting company of the aggregate property. Unless the analysis of such cost into its constituent elements can be said to be related more essentially to the original cost of the various items of property than to what they would cost currently, the question before us is settled by the order in the *Depreciation case*, because the report in that case holds that the proper basis for depreciation charges is original cost to the accounting company, or the nearest practicable equivalent. *Depreciation case*, *supra*, 424.

While other considerations may affect the price to be paid for telephone plant purchased, it is fair to assume that the parties would have in mind as one of the elements the residual value of the various items stated in terms of the current price level. At any rate that is what the vendor parts with and what the vendee acquires so far as tangibles are concerned. If the price exceeds this figure, it is natural to ascribe the excess to intangible elements and to allocate the cost to the vendee of the tangible items on the basis of what their current cost would be. On the other hand, if the price is less, the deficiency may be regarded as presenting an analogy to donations,

with respect to which we indicated under R–15 that current cost new should be the basis of the charges to the plant accounts as opposed to original cost. In this case, however, the amount of the deficiency would be credited to account 278 "Undistributed cost of property." As this is the same account to which the excess, if any, arising from other transactions would be charged, there would be a tendency toward minimizing the balance of undistributed costs of this nature.

The foregoing discussion is based upon the assumption that original cost would be susceptible of reasonable approximation. We think, however, that the practical difficulties which would ordinarily be encountered in the determination of original cost or a satisfactory estimate thereof furnish an additional reason against the adoption of the recommendation.

(3) The portion of the contra entry which would balance the credit proposed to be required to account 175 "Contributions for extensions" [Donations] could not be included in account 278 "Undistributed cost of property," or any plant account without resulting in obvious duplication. This is doubtless one of the reasons underlying the proposal to reflect items of this nature in a separate balance-sheet account [100.2] "Telephone plant purchase adjustment." But the injection of a credit entry to record a liability, as for donations, in respect of property none of which is thus acquired by the accounting company, is, of course, a pure fiction and forces a debit entry which is equally fictitious.

It is true that the tribunal having jurisdiction might prevent the necessity for any such debit entry by imposing restrictions upon the price which it would approve, to the extent necessary to effectuate a transfer of the donations to the vendee. However, the title to the donated property being in the vendor, we have no reason to suppose that in fixing the price to be paid the parties would take into consideration the fact that a portion of the property had been donated. Neither are we aware of any legal principle in opposition to the payment and receipt of a consideration for such property.

(4) All other items which, under the recommendation, would be included in account [100.2] "Telephone plant purchase adjustment," are now provided for in account 278 "Undistributed cost of property." If segregation of these items is necessary or desirable, it could be accomplished by requiring subdivision of the last-mentioned account.

(R–17) This would broaden the language of paragraph (F) of instruction 21 "Telephone plant purchased," by expressly requiring that those journal entries recording purchases that are required to be presented for our consideration and approval show also the accounting distribution. The instruction just mentioned explicitly applies to

the accounting for telephone plant purchased and prescribes the distribution to be made thereunder. It therefore appears superfluous to specify that the journal entries to be submitted in the cases covered by paragraph (F) should show the accounting distribution. In order that there may be no uncertainty, however, we hold that the language of that paragraph is to be construed as imposing this requirement.

Taken literally, the recommendation would further provide that there be submitted to us in all cases a copy of the contract of purchase, detailed statements and computations of the amounts to be set up in the plant and reserve accounts, a statement of the amounts recorded by the vendor with respect to the property, a copy of the inventory and appraisal, if any, and a copy of any order made by a State commission in connection with the purchase. We are inclined to the view, however, that it was intended to restrict these requirements to the cases covered by paragraph (F). So treating the matter, it is our opinion that except for the last-mentioned item, such of the information as is necessary is embraced by the text of that paragraph. On the other hand, we are impressed with the desirability of requiring the submission of orders made by State commissions in the premises. Accordingly, there should be subjoined to paragraph (F) the following: "A copy of the order or orders made by a State commission in connection with such purchase shall be submitted with the foregoing."

(R–18) This is a proposal to amend paragraph (A) of instruction 22 by inserting in the enumeration of major items of cost of construction of property chargeable to the plant accounts, the following: "employees' pensions and benefits" [relief and pensions], and "construction services."

The latter term is said to embrace services rendered in connection with construction, such as electric light or telephone service. A fair interpretation of the present text would include such items under the expression "other analogous elements."

It is not disputed that the element of employees' pensions and benefits, insofar as it applies to employees engaged in construction, is in theory properly includible. However, the assistant comptroller of the American Company stressed the practical difficulty of allocation and the relatively small amounts involved, and the representative of the 21 commissions indicated a readiness to yield the point. We therefore treat this portion of the recommendation as withdrawn.

(R–19) This would add to subparagraph (4) of instruction 22 (B) defining "Cost of contract work," a provision requiring that separate records be kept and separate charges made for work of this character performed by affiliated companies.

Records which are kept in sufficient detail to conform with the requirements of instruction 2, "Records," should, in the case of work performed under contract, disclose the names of contractors and the amounts respectively paid to them. The information with respect to which a separate showing is sought to be required as a matter of routine would, therefore, be susceptible of ascertainment if deemed of sufficient importance. In view of this fact and considering the additional expense that would undoubtedly be entailed, we are not impressed with the necessity or propriety of imposing the requirement proposed.

(R–20) This is a proposal to modify subparagraph (b) of instruction 22 (B) (10) by inserting the express requirement that charges to the plant accounts for interest on funds derived from the sale of securities and specifically acquired and separately held for use in construction, shall be diminished by the amount of interest earned thereon.

That such diminution is proper is not disputed. Accordingly, the recommendation should be adopted and said paragraph revised to read as follows:

(b) When funds, derived from the sale of bonds, notes, and other interest-bearing debt, are specifically acquired and separately held for use in the construction of telephone plant, the total interest, discount or premium, and expense on such debt, less interest earned on such funds, applicable to the accounting period shall be included in the cost of telephone plant and credited to account 313, "Interest income."

It is also proposed to add to the above paragraph a provision to the effect that the amounts to be thus included in the cost of plant shall not exceed reasonable interest. This is too narrow, in that it excludes the element of debt expense, but that the charges to plant on account of interest during construction should not exceed reasonable amounts is a postulate to which we readily assent. In most instances the reasonableness of such charges with respect to borrowed funds will in effect be determined by tribunals having jurisdiction over the issuance of securities. If this is not true in all cases, the remedy must be sought elsewhere, because with respect to bilateral transactions a system of accounts is concerned with what is actually paid or incurred rather than the reasonableness thereof.

(R–21) The first sentence of subparagraph (c) of instruction 22 (B) (10) now reads as follows:

During a period of suspension of a construction project no interest charge for a longer period than one year from the date of its suspension shall be included in these accounts unless specifically authorized by this Commission.

It is proposed to change this to read as follows:

Unless specifically authorized by the State commission having jurisdiction and by this Commission, no interest shall be charged prior to actual construc-

tion of the property concerned, nor shall interest be charged during a period of suspension of construction exceeding one year.

We question our power to surrender authority in part to a State commission, as this amendment proposes, and know of no good reason why this should be done in any event. Insofar as the change would preclude charges prior to actual construction, the proposal is in conflict with subparagraph (b) immediately preceding, and it appears that under circumstances covered by the latter, charges of this nature would be proper.

The recommendation is disapproved.

(R–22) This is a proposal to insert following instruction 22 a new instruction [22.1] "Overhead construction costs," which would provide: (*a*) That all such costs be charged to particular jobs or items "on the basis of the amounts of such overheads applicable thereto," in order that entire costs may be credited to the plant accounts upon retirement; (*b*) that supporting records be so kept as to show the nature of expenditures, the individual jobs and accounts charged with each kind of overhead cost and the bases of distribution, and the amounts charged to each plant account for such overhead without the necessity of detailed analysis: (*c*) that the foregoing is not to be interpreted as authorizing arbitrary percentages for assumed overhead costs, but only the assignment of actual and necessary overhead expenditures.

The degree of refinement sought under (a) is not clear, but the uniform system requires an equitable apportionment of overhead costs to plant construction. With respect to the desired precision of retirement credits, the order in the *Depreciation case* permits using averages where the use of specific amounts is impracticable. It would seem that records necessarily kept would disclose the information specified under (b), but it is to be doubted that any records would do so without the necessity of more or less detailed analysis. The sense of subparagraph (c) is in consonance with the uniform system, but in the last analysis the assignment of overhead costs is a matter largely involving the exercise of judgment. Experience may show the need for such an instruction, but we are not now persuaded that the recommendation should be adopted. Much that the State commissions may desire in this connection can apparently be accomplished through their power to require the subdivision of primary accounts.

(R–23) This is a proposal to insert in instruction 25 "Telephone plant retired," a new paragraph which, among other things, emphasizes the requirement that the cost of property retired be credited to the plant account, and states a method for determining book cost of items not separately recorded. The paragraph is essentially ad-

monitory and with one exception involves repetition of matter sufficiently covered elsewhere. The exception consists in a provision that credits which record retirements shall cite by name and page of book, or other record, the original entry of cost of the item retired, or if there is no original entry, state that fact. It is contended by the telephone companies that this requirement, which was contained in the uniform system of accounts effective January 1, 1913, cannot be followed except in a very few instances. It appears, nevertheless, that in those cases where the information can be furnished it would be useful in checking the accounts and that the proposed requirement would entail only a slight burden in addition to that already imposed by the necessity of searching the records for the original entry.

While believing that it is in large part unnecessary, we approve this recommendation and the instruction will be revised to include the following paragraph:

(aA) To the end that the telephone plant accounts shall at all times disclose the cost of all property in service, the cost of retired property, whether replaced or not, except as provided in paragraph (A) (2) below, must be credited to the account or accounts in this classification to which such cost was charged. Every company should, therefore, take such measures and establish such procedure as will insure strict compliance with these requirements. When anything is worn out, lost, sold, destroyed, abandoned, surrendered upon lapse of title, becomes permanently unserviceable or is withdrawn or retired from service for any other reason, the amount at which such thing stood charged in the plant account shall be credited to the appropriate plant account, and the entry of such credit shall cite by name and page of book or other record the original entry of cost of the thing retired. If there is no original entry that fact shall be stated in connection with the credit entry. If the amount originally charged is not separately recorded, it shall be taken to be the proportionate share of said property in the book cost, of the entire group in which the property is included.

(R-24) Subparagraph (2) of paragraph (A) of instruction 25 "Telephone plant retired," provides that the excess cost of replacing minor items shall be charged to the appropriate plant account "if the replacement effects a substantial betterment (the primary aim of which is to make the property affected more useful, of greater durability or of greater capacity)." Under the recommendation the fact that the primary aim is to make the property "more economical in operation," would constitute an additional criterion for determining the question of betterment.

It is not disputed that the idea of greater economy in operation should be thus covered if it has not already been included. It is our opinion that the words "more useful," in the sense here employed, should be construed as including any aspect of increased economy in

operation which is not covered by the expressions "greater durability" and "greater capacity."

(R–25) This proposal would modify paragraph (C) of instruction 25, "Telephone plant retired," so that in the case of land retired from telephone service and held for sale the book cost thereof shall be charged to account 103, "Miscellaneous physical property."

The effect of this revision would be to require that in all cases where such land is not sold contemporaneously with its physical retirement, it must be transferred to account 103 even though it may be held for immediate sale and be disposed of within a reasonable time thereafter. While this revision may create some slight inconvenience in accounting, it is sound in principle and we approve it. Accordingly the third sentence of this paragraph will be revised to read as follows:

If the land is retained by the company and held for sale, the book cost shall be charged to account 103, "Miscellaneous physical property."

(R–26) This modification is proposed in order to coordinate the reference made in instruction 25 (C), to the text of accounts prescribing the accounting for leaseholds retired, with the proposal to create a new operating-expense account [613] "Amortization of intangible property," in the text of which the accounting for the retirement of leaseholds and other intangible property is covered, and under which the amortization of leaseholds now chargeable to account 671, "Operating rents," would be grouped with charges for amortization of other intangible property. The latter proposal is disposed of adversely under R–100.

(R–27) The substance of this proposal, so far as material, is to subjoin to paragraph (D) of instruction 25 a provision that when classes of outside plant are subdivided between exchange and toll or by areas the bases for determining average book costs for retirement purposes shall conform with the respective subdivisions. As this measure is obviously designed to promote accuracy in retirement accounting, the textual inclusion of a statement of its purpose does not appear necessary even if it were otherwise appropriate.

The objection of the telephone companies is based upon the difficulties encountered in subdivision, but the operation of the provision is expressly confined to cases where subdivision is maintained. Viewed in this light, we think that the principle involved should be adopted. Accordingly the paragraph in question should be revised by qualifying the statement respecting average book costs, and introducing appropriate formal changes, so as to read as follows:

(D) Determination of book costs: The book cost of telephone plant retired shall be the amount at which such property is included in the telephone plant

accounts when such amount can be determined from the company's records. Ordinarily, such records shall be used in the retirement of land, buildings, complete central offices, furniture and other items of plant for which individual cost records are maintained. When the actual book cost cannot be determined from the records, it shall be estimated. When it is impracticable to determine the book cost of each item due to the relatively large number or small cost of such items, the average book cost of all the items shall be used in determining the book cost of the items retired: Provided, however, that when classes of outside plant are subdivided between exchange and toll or by areas, the bases of such average book costs shall be confined to items comprised in the respective subdivisions. This method of average book costs may be applied in retirement of such items as telephones, bell boxes, station installations, poles, cross arms, wire, cable, cable terminals, conduit, and nonmultiple private branch exchange switchboards.

(R–28) The purpose of this revision is to incorporate in instruction 25 (E) a reference to the accounting for the retirement of "Telephone plant purchase adjustment" provided in the text of proposed account [100.2], which, in our comment under R–42 we decline to adopt; also with respect to the accounting for the retirement of franchises and patent rights the purpose is to effect coordination with the proposal to create account [613] "Amortization of intangible property", corresponding with that sought under recommendation R–26 with respect to the accounting for the retirement of leaseholds. This matter is covered by our comment under R–26 and R–100.

(R–29) This involves inserting to follow instruction 25, a new instruction [26] "Work order system required", consisting of a comprehensive plan for recording changes in telephone plant including a work-order estimate and a work in progress record. The former would embrace identification of authority and project, cost estimate, accounts to be charged, variations from actual costs, and reference to records of cost of existing plant to be affected. The latter would correlate with the work-order estimates and contain accumulated charges for each project and totals for completed projects with full details of the amount concurrently carried in proposed account [100.1] "Construction work in progress". A note would provide for the suspension of the foregoing requirements in particular cases, if we are satisfied that an equivalent system is employed.

It is unnecessary to discuss the merits of the work-order system proposed, as in our opinion the recommendation concerns merely methods to be employed in complying with the requirements of the uniform system rather than basic accounting principles and should constitute the subject of separate investigation and consideration.

(R–30) Under this recommendation there would be inserted a new instruction [27] "Telephone plant, perpetual inventory required," the salient provisions of which are implied by the title. Certain features are subject to objections hereinbefore discussed. Aside from

this, we regard this recommendation as involving matter of the same nature as that immediately preceding and subject to the same disposition.

(R–31) This would amend instruction 31 "Income from sinking and other funds," by including reference to account 173, "Employment stabilization reserve," as one of the accounts that may properly be credited as a result of concurrent charges to income or surplus on account of income required to be charged to accounts covering funds represented by reserves. It will be observed that the first alternative proposed under recommendation R–74 is to abolish account 173, but that this is hereinafter rejected.

The failure to make the provision in question was not intentional and since the propriety thereof is not questioned the last sentence of the instruction should be revised in accordance with the recommendation as follows:

If such funds are represented by a reserve established through reservations of income or surplus, amounts so set aside shall be charged to account 342, "Contractual reservations of income," account 343, "Miscellaneous reservations of income," account 414, "Contractual reservations of surplus," or account 415, "Miscellaneous reservations of surplus," and credited to account 169, "Insurance reserve," account 170, "Provident reserve," account 173, "Employment stabilization reserve," or account 180, "Surplus reserved," as may be appropriate.

(R–32) This recommendation is designed to coordinate the reference made in instruction 64, "Extensive replacements," to account 138, "Extraordinary maintenance suspense," with the change of title of that account proposed under recommendation R–59 and hereinafter rejected.

(R–33) Instruction 70, "Purpose of clearing accounts", provides that items includible in a clearing account may be charged directly to the appropriate primary accounts if they can be properly allocated thereto as they are incurred. The recommendation would restrict the exercise of this option to those cases where a State commission having jurisdiction does not require otherwise.

That the direct charging of such items is not mandatory constitutes in itself an exception to the general rule. In these circumstances no sufficient reason appears why the exception should not be enlarged so that State commissions having jurisdiction will be free to require that items of the nature in question shall be handled through the appropriate clearing account.

Accordingly the substance of the recommendation should be adopted and the last sentence of the text of this instruction amended to read as follows:

Any such items which can be properly allocated to the appropriate primary accounts as they are incurred may be charged direct to those accounts unless a

State commission having jurisdiction shall require that they be accounted for through the appropriate clearing account.

(R–34) With the exception of that portion separately treated below, the effect of the proposed revision of paragraph (A) of instruction 80, "Computation and filing of depreciation rates," would be to constitute the State commissions as the tribunals to consider and determine depreciation rates except where they were without jurisdiction or declined to act, and to dispense with the issuance of temporary orders prescribing depreciation rates. The instruction in its present form is in accordance with finding 7 and the related portion of our order in the *Depreciation case*, *supra*, page 445, whereas it is apparent that the proposal in question contravenes such finding and order in the material respects above indicated.

The proposed amendment of paragraph (B) requires no comment beyond pointing out that it is correlated with that portion of the revision of paragraph (A) which contemplates the fixing of depreciation rates by the State commissions as well as by ourselves.

With respect to the foregoing the recommendation is rejected.

It is also proposed to revise paragraph (A) by inserting an express prohibition against the inclusion, in the depreciation rates to be computed and filed by accounting companies, of any allowance for the loss in service value of property expected to be installed in the future.

The record is practically devoid of any comment in this connection, but as we understand the proposal it is directed against the practice, sometimes advocated, of loading the depreciation rate for a particular structure so that the service value thereof, and that of a contemplated future addition thereto, may be distributed under the straight-line method in equal annual charges to operating expenses during the estimated service life of the structure, which but for the addition would be substantially shorter.

This practice would result in the accrual of more than the service value of the original unit during its estimated service life, in contravention of paragraph (5) of our order in the *Depreciation case*, which requires that the annual charges for depreciation be computed—

at such percentage rate of the ledger value of the property in question that the service value may be distributed under the straight-line method in equal annual charges to operating expenses during the estimated service life of the property.

On the other hand, the proposed revision is consistent with the order mentioned and tends to clarify the instruction in question, which, of course, was intended to conform with the order in all particulars.

The recommendation in this respect should, therefore, be adopted and the third sentence of the paragraph revised to read as follows:

These percentage rates shall be computed in conformity with the group plan of accounting for depreciation and shall be such that the loss in service value of the property, except for losses excluded under the definition of depreciation (note instruction 3–J), may be distributed under the straight-line method (note instruction 3–Z) during the service life of the property, and shall not include any allowance for the loss in service value of property expected to be installed in the future.

(R–35) This would amend paragraph (A) of instruction 81, "Depreciation Charges," requiring monthly accounting for currently accruing depreciation, so as to prescribe that in addition to provision afforded in that respect by account 608, "Depreciation," charges shall be made to clearing accounts generally in lieu of the present restriction thereof to account 702 of that group. This recommendation is presumably intended to coordinate said paragraph with the proposal to allocate a portion of the charges for depreciation to account 704, "Supply expense," in addition to those now included in account 702. It is rejected in accordance with our comment under R–116, wherein a similar conclusion is reached with respect to the latter proposal.

(R–36) This proposed amendment of the text of paragraph (C) of instruction 81, "Depreciation charges", is correlated with that portion of the proposed revision of paragraph (A) of instruction 80 which contemplates the fixing of depreciation rates by the State commissions, as well as by ourselves. For the reasons stated in our comment under R–34 the recommendation is rejected.

(R–37) This would add to the text of instruction 82, "Classes of depreciable telephone plant", a note providing that when depreciable plant is distributed from account 276, "Telephone plant purchased", adjusting entries shall be made covering depreciation applicable thereto while carried in the account mentioned. Under the uniform system this result is intended to be accomplished through note B following the text of account 276. In its present form that note covers the substance of the proposal and its position appears to be no less appropriate.

(R–38) Under this recommendation the use of account 138, "Extraordinary maintenance suspense", in order to avoid undue diminution of the depreciation reserve where the cause of retirement is not a recognized factor in depreciation and the loss is not covered by insurance, would be conditioned upon approval not only of ourselves as now provided, but also of any State commission having jurisdiction. This point, and also the proposal to change the title of account 138, are disposed of adversely in our comment under R–59.

The further proposal with respect to the necessary approval of the period over which distribution may be made from account 138 to operating expenses is analogous to that first above mentioned and it is accordingly rejected.

(R–39) This involves proposed changes in the balance-sheet statement appearing at page 22 of the uniform system in harmony with recommendations affecting the texts of the several accounts, and is therefore sufficiently covered by comments hereinafter made in that connection.

(R–40) This would amend the text of account 100, "Telephone plant", so as to provide that it shall include the *cost* of the company's property used or held for telephone service instead of the company's *investment* therein.

Instruction 21 and the text of account 202, "Franchises", provide for the inclusion of the *original cost* of franchises acquired by assignment. However, if the word "cost" in the proposed revision is intended to mean original cost as applied to all property, the matter is sufficiently covered by our comment under R–13. The latter also shows that although cost to the accounting company is the fundamental basis prescribed for charges to the plant accounts, it is not strictly applicable in all instances where physical property is acquired.

Since the instructions clearly prescribe what is to be charged to the several plant accounts into which the total of account 100 is classified, it is our opinion that the more comprehensive term "investment" is preferable to that recommended.

(R–41) Under this recommendation, account 280, "Construction work in progress", would be transferred from the plant accounts to the balance-sheet group under number [100.1].

The effect of this would be to exclude from account 100, "Telephone plant", property actually held for telephone service and constituting telephone plant under instruction 3, "Definitions", (BB), to which reference is made under R–11. The object of the recommendation is to facilitate a separation, for rate-case purposes, between property actually devoted to telephone service and property subject to the accrual of interest during construction. This is now accomplished through note B to the account under discussion, which requires that the balance therein shall be shown separately under account 100 in the short column of the balance-sheet statement in the company's annual report to us.

For the reasons stated the recommendation is rejected.

(R–42) This would create a new balance-sheet account [100.2] in which to include, as items of "telephone plant purchase adjust-

ment", a portion of the information for which provision is now made in plant account 278, "Undistributed cost of property." The purpose of the recommendation is to eliminate from investment in telephone plant the difference between the price paid in the purchase of such plant and the original cost thereof, less requirements for depreciation and amortization reserves, and the applicable portion of the amount carried on the books of the vendor to record the liability for donations. It is urged that such difference, if a debit, should not constitute a portion of the depreciation base and further that it is not represented by any plant at all.

As indicated in our comment and conclusion under R–40, account 100 should include the accounting company's *investment* in property used or held for telephone service. Since the purchase price of such property constitutes investment therein, it should be included in account 100, irrespective of questions relating to its propriety as a depreciation base or its susceptibility of assignment to the primary plant accounts other than residual accounts.

It follows that any difference between the purchase price and the net of the amounts assignable to account 211, "Land", the depreciable plant accounts, account 202, "Franchises", account 232, "Station installations", account 233, "Drop and block wires", "Construction work in progress", and the reserve requirements applicable to the plant, is itself chargeable as a plant-account item and should be included in account 100.

It may be remarked in passing that proposed paragraph (C), which provides that the amounts in question shall be disposed of or amortized in such manner as the commission having jurisdiction may direct, involves unauthorized delegation of power to the State commissions.

Accordingly the recommendation is disapproved.

(R–43) This would prescribe that there be included in account 101, "Investments in affiliated companies", the *cost* (*except as provided in instruction 12–B*) of the company's investment in securities coming within the description in the text. The present wording is "book cost" (with a reference to instruction 12), which expression is defined generally in instruction 3, "Definitions", (E), and, as applied to securities, in the instruction above referred to. The latter provides that the book cost of securities is to be determined by the current money value of the consideration given therefor and in paragraph (B) the option is accorded of writing down the book cost in recognition of depreciation in value. This undoubtedly accounts for the choice of wording which is advanced, but as indicated in our comment under R–7, "book cost" is a concept of a current nature and serves equally well.

It may be that reliance is also placed upon the following points made in the memorandum of the 10 commissions, namely, (*a*) that since book cost is by definition the amount at which the item is carried on the books, to say that the account shall include the book cost is traveling in a circle, (*b*) that book cost is not adequately defined.

The first point overlooks the fact that one of the fundamental requirements of a system of accounts is to prescribe *where* the various items shall be included.

The second point is sufficiently answered by reference to the instructions above mentioned and to instruction 20 which defines the amounts chargeable to the plant accounts.

(R–44) (R–45) (R–48) The purpose of these recommendations is to eliminate from account 101, "Investments in affiliated companies", the amount of investment advances to such companies, to set up the latter in a separate balance-sheet account [101.1], "Advances to affiliated companies", and to refine the separation now prescribed in paragraph (B) of account 101, as between stocks, funded debt, and investment advances, so that stocks will be segregated into common and preferred.

These recommendations as well as others relating to balance-sheet accounts exhibit a tendency toward reversal of the normal trend of the balance sheet, which is directed to consolidation of similar items rather than detailed analysis.

In our forms for annual reports of class A telephone companies, we have incorporated schedules calling for the details of the subaccounts above mentioned. The schedule for stocks and funded debt requires the statement of the name of each issuing company, a description of the security, and a separation as between pledged and unpledged securities. That for investment advances requires a separation between affiliated companies and others, including the statement of the name of the debtor company and the amount of advances at the close of the year. In view of these requirements and the availability of the records which must be kept in order to comply therewith, the necessity for the recommended accounting revisions is not apparent.

(R–46) This recommendation would eliminate from paragraph (C) of account 101, the note styled A, relating to amounts receivable from affiliated companies which are subject to current settlement. As the substance of this note is proposed for inclusion under account [101.1] "Advances to affiliated companies", the recommendation is rejected in accordance with our comment under R–44, R–45, and R–48.

(R–47) This involves the elimination, from paragraph (C), account 101, of the note styled B, relating to borrowed securities. This note is designed to prevent the inclusion in the balance sheet of contra entries recording liabilities with respect to borrowed securities which, so far as being expressed in money is concerned, are merely contingent. Accordingly the recommendation is disapproved.

(R–49) This would involve an amendment of the text of paragraph (A) of account 102, "Other investments," identical with that considered under R–43, and the comment there made is applicable here.

(R–50) The scope of account 103, "Miscellaneous physical property," is defined in the uniform system by antithesis to telephone plant aided by a parenthetical reference to the account in which the latter is included. The proposed revision would expand this reference to include the suggested new balance-sheet accounts [100.1] "Construction work in progress," and [100.2] "Telephone plant purchase adjustment." While our rejection of the latter proposals under R–41 and R–42 thus determines the present question, it is interesting to note that the recommendation implies agreement with our theory that these proposed balance-sheet accounts cover telephone plant and not miscellaneous physical property.

The proposed revision whereby land other than that for which there is a definite plan for its use in telephone service *within one year*, should, when acquired, be included in account 103 together with buildings and improvements thereon, is sufficiently covered by our comment under R–11.

It is further proposed to amend the text of this account by eliminating the words "and held other than for immediate sale," which qualifies the provision for the inclusion of land (with buildings and other improvements thereon) retired from telephone service, and by striking the note which provides for the retention thereof in accounts 211 and 212 when held for immediate sale. This amendment has been covered by our comment under R–25, and is approved. Accordingly the note will be canceled and the second sentence of the text of this account will be revised to read as follows:

> It shall include the cost of land when acquired other than that for which there is a definite plan for its use in telephone service and buildings and other improvements upon such land, also the cost of land retired from telephone service, and buildings and other improvements upon such land.

(R–51) The proposed substitute for book cost is sufficiently covered by our comment under R–43.

In harmony with the proposed general scheme of segregating obligations of affiliates, this recommendation is designed to exclude from

account 116, "Temporary cash investments", all securities of affiliated companies. It appears, however, to be desirable for administrative purposes to include in one account all temporary cash investments and no adequate reason has been advanced for the creation of an exception in those instances where a company may elect to invest its cash temporarily in the securities of affiliates.

The reference to instruction 13 should not be eliminated, because it directs attention to the fact that company securities owned are not to be included.

(R–52) (R–53) The proposed revision relating to book cost is sufficiently covered by our comment under R–43.

The object of these recommendations is to effectuate a subdivision of account 117, "Notes receivable", so that obligations of affiliated companies of the nature comprehended by the present text will be included in a proposed separate account [118.1], "Notes receivable from affiliated companies".

All the information that would be included in the latter account must be separately shown in the companies' books. As we have pointed out elsewhere herein, the opportunity to require subdivision is open to those State commissions having jurisdiction. Independently of that, however, we have incorporated a schedule in our forms for annual reports of class A telephone companies which requires an analysis of account 117 to show a separation between notes receivable from affiliated companies and from others. The proposed revision does not appear to be warranted.

(R–54) (R–55) The purpose of these recommendations is to effectuate a subdivision of account 120, "Accounts receivable," corresponding with that sought by recommendations R–52 and R–53 with respect to account 117, "Notes receivable." Our comments in the latter connection are applicable here, including, with appropriate formal modifications, the reference to our annual report schedules.

(R–56) This involves amending the text of paragraph (A) of account 122, "Material and supplies," so as to cover the cost of *materials* in addition to articles in process of manufacture, and to introduce expressly the requirement of ownership by the company as a prerequisite to inclusion in either case.

With respect to the latter matter, the telephone companies take the position that it is too narrow in that it would exclude advance payments and payments made on account of conditional sales. Items of this nature should be included because, under the text in question, and that of instruction 10, "Purpose of balance-sheet accounts," we are dealing with cost as representing assets of the accounting company. Furthermore, these provisions should be construed as confining the scope of this account to the company's interest in property

in process of manufacture, without the aid of the proposed revision. There is no dispute concerning the first portion of the recommendation and it appears that the term "articles" is not sufficiently comprehensive. Accordingly the paragraph should be revised to read as follows:

(A) This account shall include the cost of unapplied material and supplies held in stock, including plant supplies, tools, fuel, stationery, directory paper stock, and other supplies, and materials and articles in process of manufacture for supply stock.

(R–57) This involves the creation of a new balance-sheet account [122.1], "Subscriptions to capital stock", for the inclusion of the balance due upon legally enforceable subscriptions to capital stock. Presumably the words "legally enforceable" have reference to the form of the contract and apply to subscriptions not known to be unenforceable in fact.

While obligations of this character are sometimes considered as assets to be included as such in the balance sheet, they are of such an inceptive, if not contingent, nature that under proper accounting their inclusion in the balance-sheet totals is not warranted. However, the disclosure of the material facts respecting subscriptions to capital stock is required by paragraph (C) of account 153. "Capital stock installments", which provides that there be shown in the short column of the balance sheet the total amount of capital stock subscriptions which have not been fully paid or canceled and also the total amount unpaid on such subscriptions.

The supporting details proposed to be required would, as a matter of practical necessity, be contained in records kept in conformity with requirements of the uniform system and those pertaining to annual reports.

The recommendation is, therefore, rejected.

(R–58) This is a proposal to segregate from account 201, "Organization", all expense connected with the issuance and sale of capital stock and include them in a new balance-sheet account [134.1], "Capital stock expense". The effect of this would be to treat such expenditures as deferred debits rather than items of permanent investment. In our opinion this would not be proper because they represent something in the nature of intangible assets which, while subject to the possibility of retirement, have a probable existence of indefinite duration. Furthermore, expenditures of this character are relatively of minor importance and their connection with the cost of organization is logically almost inseparable.

The provisions of proposed paragraph (B), which relate to the retirement of capital-stock expense applicable to superseded or canceled stock, are in substance embodied in note A to account 201.

In view of the nature of the items in question, amortization thereof as provided in proposed paragraph (C) would not be appropriate in the absence of special circumstances.

We regard as unnecessary the proposed note following the list of items, which would expressly provide for the inclusion in account 413, "Miscellaneous debits to surplus", of expenses in connection with the reacquisition and resale of stock. Any special expense of reacquisition should be so charged in accordance with instruction 40 (d) and the text of account 413, particularly the eleventh item thereunder. The text of that account and the instruction referred to would also require similar treatment of any special expense of resale other than discount, which would be includible in account 134, "Discount on capital stock", in accordance with instruction 14 (A).

In view of the foregoing the recommendation is rejected.

(R–59) Under this recommendation it is proposed to substitute the word "retirement" for the word "maintenance" in the title of account 138, "Extraordinary maintenance suspense."

The text of this account embraces the cost of certain extensive replacements, i.e., maintenance, as well as retirement expenses growing out of special circumstances. There is thus little choice when the words are considered in their specific senses. However, since maintenance is the more general term, it is in our opinion preferable.

It is further proposed to amend paragraph (C) so as to restrict the use of this account to instances where permission has been obtained not only from ourselves as now provided, but also from any State commission having jurisdiction. Such a provision involves the unauthorized surrender of power to the State commissions.

(R–60) Under this recommendation, the application of that portion of the text of account 139, "Other deferred debits," which provides for the inclusion of the cost of preliminary surveys, plans, investigations, etc., made for determining the feasibility of projects under contemplation, would be confined to engineering items.

The provision in question should be construed as including such items. We think, however, that the proposal is too narrow, in that it would tend to exclude analogous items, such as traffic surveys, etc.

It is further proposed to eliminate the word "other" from the following clause: "if other contemplated projects are carried out, the preliminary costs shall be included in the cost of the projects;" and to commence the final sentence of the text with said clause as amended.

The word "other" is used in contradistinction to contemplated purchases or sales mentioned immediately preceding. An apparent ambiguity may be raised by assuming that "other" is used in

contrast with previously contemplated projects not carried out, from which it might be inferred that the preliminary costs thereof are to be included in the cost of those that are carried out. This, however, is negatived by the following clause, which refers to all contemplated projects (including purchases and sales) and provides as follows:

> if the contemplated projects are abandoned, such costs (including options paid, if any) shall be charged to account 413, "Miscellaneous debits to surplus."

In our opinion, the proposed revision fails to clarify or adequately cover the situation.

(R–61) Proposes the amendment of the text of paragraph (A) (1) (c) of account 150, "Capital stock", by adding the words shown in italics so as to provide that there be included therein, as book liability with respect to stock actually outstanding: "Appropriations of surplus which have been transferred to nonpar stock account *with the approval of the State commission having jurisdiction.*" This revision is bad in form because it excludes specific provision for those cases arising without the suggested approval. It is bad in substance for the reasons given in our comment under R–12.

(R–62) Under this recommendation amount 153, "Capital stock installments", would be eliminated and there would be created two new balance-sheet accounts [152.1], "Capital stock subscribed", and [153], "Installments paid on capital stock".

The first of these proposed accounts is designed for the inclusion of the subscription price of unissued stock with respect to which the subscriptions are legally enforceable. Presumably the last two words have the same meaning here as in recommendation R–57. The effect of this proposal would be to set up amounts as capital-stock liability, the total of which in some cases, and part of which in all cases, is yet to be paid into the enterprise, and with respect to which the liability is of a contingent nature. As indicated in our comment under R–57, we do not regard this as proper accounting, but the total amount of capital-stock subscriptions which have not been fully paid or canceled is required to be shown in the short column of the balance sheet.

It is true that this account, taken in connection with that proposed under recommendation R–57, would afford a segregation of part of what is now required to be included under effective account 153, in that the difference between the balances shown therein would represent the amount of installments paid under contracts in form enforceable. However, if this information is desired, an appropriate subdivision of effective account 153 would disclose it.

The second of the accounts proposed hereunder is designed for the inclusion of the amount of installments paid on so-called subscrip-

tions to capital stock not constituting legally enforceable contracts. It would thus comprise the residue of account 153, "Capital stock installments". The latter account is intended to include all of the installments paid on account of subscriptions to capital stock, for which stock has not been issued, and in our opinion that is the extent of the liability that should be recorded as such on account of stock subscriptions.

The statement made in our comment under R–57 respecting the supporting details proposed to be required is also applicable here.

For the reasons stated the recommendation is rejected.

(R–63) This is designed to coordinate with recommendations R–66 and R–67 the note directing the inclusion elsewhere of amounts due affiliated companies subject to current settlement, which appears under account 156, "Advances from affiliated companies." In this aspect the matter is covered by our comment upon the proposed revisions above referred to.

The recommendation, by confining its reference to the two proposed accounts, [159.1] and [159.2], would also have the effect of requiring the exclusion of items comprehended by the note from accounts which might be more appropriate. For example, amounts currently due to others for telephone service are now includible in account 159, "Accounts payable." Such items due affiliated companies, it will be observed, are expressly excluded from the proposed account [159.2], "Accounts payable to affiliated companies," and would therefore be includible under account 165, "Other current liabilities."

(R–64) (R–65) (R–66) (R–67) The purpose of the first and third of these recommendations is to effectuate a subdivision of account 158, "Notes payable." and of the second and fourth, a subdivision of account 159, "Accounts payable," corresponding with that sought by recommendations R–52 and R–53 with respect to account 117, "Notes receivable." Our comments in the latter connection are applicable here, including with appropriate formal modifications, the reference to our annual report schedules.

(R–68) Proposes adding to account 160, "Customers' deposits", a note providing that unclaimed deposits shall be carried therein until other disposition is authorized by the State commission having jurisdiction or this Commission, or until they may devolve to the State.

We do not understand that the liability to refund unapplied balance of customers' deposits or the succession to the right to enforce the same is affected by the method of accounting prescribed therefor. Moreover, the transfer of portions of such balances to surplus as unclaimed deposits after the lapse of such time as is reasonably necessary to create a presumption that they are of such character

involves a proper recognition of their change in status as well as convenience in accounting.

The first of the alternative limitations proposed is improper, in that it involves, by implication, an unauthorized delegation of power to the State commissions. The second alternative is unnecessary, because in any case where the State might be the legal successor to unclaimed customers' deposits, it must be presumed that the law would operate without regard to the particular account in which the item might be lodged.

For the reasons first above indicated, both clauses are unreasonable as unduly restricting proper and convenient accounting practice.

(R–69) This recommendation is designed to coordinate the reference made, in paragraph (B) of account 170 to account 672, "Relief and pensions", with the proposed change of title of the latter account, which is rejected in our comment under R–107.

(R–70) This would involve a revision of the text of paragraph (A) of account 171, "Depreciation reserve", similar to that considered under R–35, and the adverse disposition there made is applicable here.

(R–71) The effect of this proposal would be to coordinate the reference made, in paragraph (B) of account 171, to account 138, "Extraordinary maintenance suspense", with the proposed change of title of the latter account which we rejected in our comment under R–59.

(R–72) This recommendation is designed to coordinate paragraph (A) of account 172 "Amortization reserve", with the proposal to create a new operating-expense account [613], "Amortization of intangible property", which is rejected in our comment under R–100.

(R–73) It is proposed by this revision of paragraph (C) of account 172, "Amortization reserve", to require that, instead of being included in surplus, adjustments for profit and loss on retirement of leaseholds, franchises, and patent rights, shall be made through the operating-expense account to which accruals for amortization thereof are charged. To do otherwise it is said would be inconsistent and unfair to subscribers.

This contention, however, overlooks the fact that in most, if not all, cases, the necessary adjustments are to be ascribed to fluctuation in market value rather than to any uncertainty as to the proportion of book cost properly allocable to the accounting periods involved. Hence, the adjustments represent capital, rather than operating, losses or gains and are properly includible in surplus.

(R–74) This is a recommendation to eliminate account 173, "Employment stabilization reserve" which covers credits corresponding

with charges concurrently made to account 611, "Employment stabilization" and to account 672, "Relief and pensions" under provisions of paragraph (F) of the latter, or in the alternative to subjoin a note conditioning the use of said account upon approval both of ourselves and the State commission having jurisdiction. The latter involves the unauthorized surrender of power to the State commissions.

The necessity for and propriety of this account are dependent upon the retention of the provisions respecting the inclusion of the corresponding charges. Since we are rejecting under R–101 and R–107, respectively, the proposal to eliminate account 611 and that portion of account 672 above mentioned, the first alternative under discussion is also rejected.

If the duration of the proposed period of accrual is such as to warrant consideration of the question of interest on the funds represented thereby, we are in a position to prescribe appropriate accounting therefor as a condition to our approval of the use of the accounts to which the accruals would be charged.

The proposal to amend the reference, made in paragraph (B), to account 672, "Relief and Pensions" is made for the same purpose as that mentioned under R–69.

(R–75) Under this recommendation it is proposed to rewrite the text of account 175, "Donations", and change the title to "Contributions for extensions". It is said that the present title is misleading in that it connotes absence of consideration. The term "donation" does not necessarily import a pure gift. It includes what is called the "onerous donation", 28 *C. J.* 621. Generally speaking, the transactions in question are of the latter class. In any event the term "contribution" is not an improvement.

The scope of the proposed account is defined by paragraph (A) as embracing—

> contributions to the company by subscribers, governmental bodies, or organizations, of labor, property, or money, made for the purpose of establishing, extending, or improving the service rendered by the company, when such contributions are not subject to refund.

In thus specifying all those who ever, as a practical matter, make "donations" to telephone companies and all possible varieties of such "donations", the proposed substitute includes no more than is covered in general terms by the effective text. In making this statement we have not overlooked the apparent scope of the words used in specifying the purposes covered, but unless the donation is in the form, or for the construction, of *plant* to be used in establishing, extending, or improving the service, it would be excepted from inclusion by the second sentence of proposed note A.

Paragraph (A) would also require that records be so kept that the amount and description of each contribution, together with the location and description of property to which it relates, will be readily available. To the extent that compliance with these requirements is reasonably possible, records kept in conformity with the provisions of the uniform system will furnish the information. It is not to be expected, however, that donations of money would be precisely identifiable with particular items of property. Moreover, when plant is donated, not only does its essential identity gradually disappear as a result of natural processes but as a practical matter it becomes merged into the whole mass of plant and is ultimately represented by other items or even by other kinds of assets.

The effective text requires that the amount of donations be permanently carried in this account, whereas proposed paragraph (B) provides that no debits shall be made thereto except when the service in connection with which the contribution was made is permanently discontinued by the company because of sale of that portion of the business or otherwise. Under the uniform system, the retirement of plant (including such as may have resulted from donations) is, with minor exceptions, met by reserves accumulated through charges to operating expenses and is, therefore, accompanied by a reduction of reserve liabilities. Thus even though the item represented a donation the liability for donations remains undiminished and balances assets into which the retired plant has in effect been transmuted.

Of course, the effective text is not intended to prevent the closing of this account in case of liquidation of the company's affairs. It is, moreover, conceivable that the circumstances presented by a partial liquidation might justify writing down the liability for donations definitely identifiable with the property disposed of and the business discontinued. However, we do not deem it advisable to make general provision for contingencies of this remote character.

The portion of proposed note A that deals with conditional contributions is in substance embodied in the note to instruction 20 (C), to which reference is made in the effective text of this account.

The remainder of this note would provide that donations to cover current operating expenses or deficits be credited to account 402 "Miscellaneous credits to surplus". In our opinion such donations are in substance revenue and should be credited to account 506, "Other local service revenues", or 516, "Other toll service revenues", as may be appropriate, in accordance with instruction 50 (B) (2).

The propriety of proposed note B is covered by our comment under R–15.

The telephone companies, while opposing the recommendation under discussion, do not appear to be entirely satisfied with the

effective text. They would assimilate all donations to forms of contribution to operating revenues or reimbursement of operating expenses. We conclude that the present distinction should be preserved, and do not anticipate that serious difficulty will arise in applying it.

For the reasons given, this recommendation is rejected.

(R–76) This recommendation involves merely the elimination of account 280, "Construction work in progress", from the list of telephone-plant accounts appearing on page 39 of the uniform system in conformity with the proposal to transfer it to the balance-sheet group as number [100.1], which is rejected in our comment under R–41.

(R–77) (R–79) These recommendations have to do with the proposal to segregate from account 201, "Organization", and include in proposed account [134.1], "Capital stock expense", all expenses connected with the issuance and sale of capital stock, which we rejected under R–58.

(R–78) (R–80) Under these recommendations, the sixth item listed under the text of account 201, "Organization", would be amended by eliminating the italicized words in the following statement: "Office expenses incident to organizing *and preparing* the company *for operation*." The record affords no explanation of this proposed change and its purpose is obscure. It is possible that the purpose is the same as that of recommendations referred to under R–77 and R–79. In any event, the matter under discussion is confined to office expenses in connection with the company, i.e., the corporate organism as distinguished from its property. We do not consider that the present statement of the items is unduly broad.

The further proposal to eliminate effective note A, the substance of which is embodied in paragraph (B) of the text of proposed account [134.1], "Capital stock expense", should be rejected in view of our decision under R–58.

In connection with the proposal to eliminate effective note B, which prohibits carying over the organization expense of former companies in case of merger, consolidation, or reorganization, except where it is clear no duplication would result, there is submitted a new note C, which embodies the substance of the foregoing, omitting the exception. The purpose of the effective note is to prevent duplication, and if it is clear that such will not be occasioned, the exception is justified.

Proposed note A, aside from provisions correlated with recommendation R–58, is designed to point out that provision is made elsewhere for the inclusion of discounts upon securities and debt expense. In this respect, it does no more than is accomplished by the present reference to instructions 14 and 15.

Proposed note B, which would provide for including in account 664, "Law department", the cost of preparing and filing papers to procure extensions of the term of incorporation, except where the first costs have been written off, appears to be unnecessary in view of the obvious construction of the purview of that account, the implications arising from analogies presented by provisions of effective notes A and B to account 201, and the recognized fundamentals of accounting.

For the reasons given, these recommendations are rejected.

(R–81) Proposes amending the text of paragraph (A) of account 211, "Land", so as to provide, as a prerequisite to the inclusion therein of the cost of land, leaseholds, etc., that such property be *used* rather than *held* for the telephone purposes enumerated. In harmony therewith it is also proposed to eliminate the following provision:

> including the cost of land for which there is a definite plan for its use in telephone service but only after the completion of telephone facilities thereon.

This language corresponds with the provision of account 280, "Construction work in progress", relating to the transfer of the cost of property to the appropriate plant accounts upon completion of construction.

If we consider the recommendation in connection with related proposals, the effect would be to require the exclusion of the cost of property answering the description above set out from proposed account [100.1], "Construction work in progress", and the inclusion thereof in account 103, "Miscellaneous physical property", in the absence of a definite plan for use *within one year*. In case such plan existed it is doubtful where the item would be included.

In view of the foregoing and of our comment under R–11 the recommendation is rejected.

(R–82) This recommendation involves amending paragraph (B) of the text of account 212, "Buildings", so as to require a definite plan for use in telephone service *within one year* as a prerequisite to the inclusion therein of the apportioned cost of buildings acquired in conjunction with land. In view of our comment under R–11 the proposal is rejected.

(R–83) The portion of this recommendation which would make the use of account 276, "Telephone plant purchased", mandatory in the case of all purchases is rejected, in accordance with the first subdivision of our comment under R–16.

The proposal to amend the text so as to provide expressly that the amount to be included shall be cost *to the accounting company* is unnecessary in view of instruction 20 (B) which, with exceptions not material in this connection, provides that the amounts charge-

able to the plant accounts shall be actual money costs to the company or the current money value of other considerations given.

The further proposal to provide for ultimate distribution *to other accounts*, as well as to plant accounts, is likewise unnecessary, because the text does not provide for the inclusion of anything but the cost of telephone plant.

It is also proposed to eliminate note A, which permits distribution (from account 276) to the primary plant accounts on the basis of estimates subject to appropriate adjustment when final data become available. We have difficulty in understanding why there should be any objection to this provision, except on the theory that it authorizes direct charges to the primary plant accounts without using account 276. The point involved is covered above. No reason is perceived for supposing that the general expression "appropriate adjustment" will lead to difficulties. We conclude that the note in question is proper.

(R–84) This would eliminate note A to account 277, "Telephone plant sold," which authorizes credits to the primary plant accounts on the basis of estimated book cost subject to appropriate adjustment when final data become available.

As indicated by their respective titles, account 277 is the counterpart of account 276. Note A to the former corresponds with note A to the latter which, in our comment under R–83, we declined to eliminate. That decision is applicable here.

(R–85) The effect of the proposed amendments to the text of account 278, "Undistributed cost of property," is to restrict its scope to those costs carried in superseded account 204, "Other intangible capital," as of December 31, 1932, which are not assignable to other primary accounts or to the proposed account [100.2], "Telephone plant purchase adjustment." Our adverse conclusion under R–42 with respect to the latter, and the third and fourth subdivisions of our comment under R–16 dealing with the same proposal in connection with account 278, lead to the rejection of the foregoing.

The proposal to amend the effective note to this account so as to include provision for apportionment of employees' pensions and benefits is similar to that disposed of under R–18.

It is further proposed to subjoin a note B to this account which would require that before any charge is made thereto a complete statement of reasons therefor, together with copy of the proposed entry, shall be submitted to any State commission having jurisdiction and to this Commission. Inasmuch as this note when considered in connection with the recommended change in the text of this account relates only to the entry bringing forward the balance from

account 204, "Other intangible capital," no good purpose can be accomplished by including it in the accounting rules.

(R–86) In addition to the recommendation to transfer account 280, "Construction work in progress", to the balance-sheet group, which we rejected in our comment under R–41, it is proposed to amend the text of paragraph (A) so as to require a definite plan for use in telephone service *within one year* as a prerequisite to the inclusion of the cost of land. This point is sufficiently covered by our comment under R–11.

It is also proposed to add to paragraph (B) a provision that "in no case shall any amount be carried in this account at the end of any month for plant which is actually in service": There is apparently no necessity for this, inasmuch as the effective text requires that when *any* telephone plant, the cost of which has been included in this account, is completed ready for service, the amount of such cost shall be credited thereto.

The further proposal to eliminate note B, which requires that the balance in this account shall be shown separately under account 100 in the short column of the balance-sheet statement in the annual report, is presumably contingent upon the transposition of the account itself. This recommendation is therefore rejected.

(R–87) Proposes substitution of the more general term "clearing account" for "account 702" in note C to account 303 "Rent for lease of operating property", which provides that when the lessee is responsible for depreciation of telephone operating property leased as a whole its accounting therefor shall conform with the basis prescribed for owned property. The recommendation is designed to correlate the scope of this note with the proposed amendment of instruction 81 "Depreciation charges", which was disposed of adversely under R–35 in accordance with the rejection under R–116 of the proposal to allocate a portion of the charges for depreciation to clearing account 704, "Supply expense".

(R–88) This would amend the text of paragraph (A) of account 313, "Interest income", so as to exclude therefrom interest on bank balances, certificates of deposits, open accounts, and other analogous items.

As indicated by the correlative proposal under R–93, the recommendation proceeds upon the assumption that these funds are used in telephone operations, from which the conclusion is drawn that interest on the funds amounts to operating revenue. This presents another aspect of the endeavor to adapt the uniform system to the requirements of rate investigations in minor particulars.

The proposal is too broad in that portions of the balances upon which the interest sought to be excluded is earned would ordinarily

represent funds in excess of those used in telephone operations. It follows that compliance with the underlying theory would necessitate current or periodic ascertainment, in the nature of a working capital determination, of the amount of each such fund used in telephone operations. Obviously, this would not be practical from the accounting standpoint. On the other hand, if the inquiry were deemed material in a particular case, it would be feasible to make such determination covering any given period and apply the results thereof to an analysis of account 313 for the corresponding period.

Without passing upon the manner in which the income in question should be treated for other purposes, we conclude that its intrinsic character justifies our classifying it, for accounting purposes, as interest rather than as revenue from telephone operations.

(R–89) The second item in the list following the text of account 323, "Miscellaneous income charges", provides for the inclusion of membership fees and dues in associations not directly or intimately related to telephone operations. This is correlated with items listed under the texts of accounts 661, "Executive department", 662, "Accounting department", 663, "Treasury department", and 664, "Law department", which provide for including in these accounts membership fees and dues of the respective departmental officers and employees in associations. In each case a note referring to account 323 directs attention to the fact that such expense charges must pertain to associations directly or intimately related to the telephone operations of the company.

With the declared object of extending and more precisely defining the scope of account 323 in this respect, it is proposed to amend the first-mentioned item so as to include therein all such fees and dues except those of the company in telephone-company associations and those of employees in professional organizations. In this connection it is also proposed under recommendations R–102 and R–112 to eliminate the items and notes under the departmental accounts above mentioned and to insert in the list following the text of account 675, "Other expenses", an item calling for the inclusion of membership fees and dues of the company in associations of telephone companies and of employees in professional organizations.

Inasmuch as the circumstances surrounding memberships and dues of telephone companies in other than telephone-company associations might conceivably justify the inclusion of the cost thereof in operating-expense accounts, the limited scope of the first excepting clause of the proposal under discussion makes the item itself too broad with respect to account 323. On the other hand we doubt that professional organization memberships and dues of employees other than those connected with the several departments above men-

tioned would be so related to telephone operations as to justify the inclusion of the cost thereof in operating expenses. This, however, would be permitted under the second excepting clause. It appears that the effective provision is the more logical and that the supposed difficulty in applying it does not justify the substitution. Furthermore, the proposal to include all the items chargeable to operating expenses in account 675 instead of classifying them as now provided would violate one of the important principles underlying the uniform system.

For the reasons stated the recommendation is rejected.

(R–90) Under this recommendation it is proposed to eliminate from the list following the text of account 402, "Miscellaneous credits to surplus", the tenth and eleventh items which provide for the inclusion of profit derived from the sale of unexpired leases, and unclaimed cutomers' deposits, respectively.

With respect to the former the recommendation is rejected in accordance with our decision under R–73; with respect to the latter, it is rejected in accordance with our comment under R–68.

(R–91) The tenth item in the list following the text of account 413, "Miscellaneous debits to surplus", provides for the inclusion of contributions for charitable, social, or community welfare purposes, not directly or intimately related to protection of the company's property, development of its business, or the welfare of its employees. This is correlated with the fourth item in the list following the text of account 675, "Other expenses", which provides for inclusion of contributions of this character when the above-mentioned direct or intimate relation exists. Note D to the latter account directs attention to the fact that in the absence of such relation the contributions shall be charged to account 413.

On the ground that the scope of account 413 is thus unduly narrowed in this respect and that of account 675 made too broad, it is proposed to amend the first-mentioned item by eliminating the qualifying clause and modifying the substantive portion so as to cover generally *donations* or contributions, including those made for the purposes enumerated. In this connection it is also proposed under recommendations R–110 and R–113 to eliminate the item and note to account 675 above mentioned. The thought is expressed that the introduction of the word "donations" conveys added significance. As used in the business world, however, any distinction between that term and "contributions" based upon qualitative difference between the consideration for either or the supposed absence thereof in the case of the former, would appear to be overdrawn. Moreover, we do not apprehend that a pure gift could be connected with operating expenses.

The effect of the recommendations would be to exclude all contributions of the character in question from operating expenses and to include them in surplus. This is contrary to the theory involved in our recent decision in *Accounting of New York Telephone Co., supra.* In that case we considered fully the question of whether a contribution to an emergency unemployment relief fund should be charged to expense or surplus, and for the guidance of telephone companies in the future maintenance of their accounts we stated a corollary to our opinion and finding, from which the language of the effective provisions here under consideration was taken. We are not persuaded that any departure therefrom is necessary.

The further proposal to add to the amended item under account 413 a parenthetical reference to account 672, "Employees' pensions and benefits", [Relief and pensions], is presumably made for the purpose of directing attention to the fact that certain donations or contributions of a restricted character would nevertheless be chargeable to operating expenses. Under the disposition above made the necessity for such reference is not apparent.

(R–92) This would amend account 413, "Miscellaneous debits to surplus", by inserting in the list following the text an item calling for the inclusion of losses of funds due to bank failures.

The recommendation is too broad in that it would cover losses of *current* funds which, in our comment under R–111, we decline to exclude from account 675, "Other expenses". We readily assent, however, to the proposition that losses of *general* funds as a result of bank failures cannot be attributed to telephone operations. In view of instruction 40, "Purpose of surplus accounts", and the text of account 413, such losses are clearly includible in the latter, so that to the extent the recommendation is otherwise proper it appears to be unnecessary.

This recommendation also directs attention to the unintentional omission of the word "of" in the fourteenth item of the list above mentioned. In accordance therewith this item should be revised to read as follows: "Inventory and appraisal costs taken incident to the purchase, sale, or lease of property where the transactions are abandoned."

(R–93) Proposes amending the text of account 526, "Other operating revenues", so as to provide for the inclusion of interest on funds used in telephone operations. This recommendation correlates with that considered under R–88 and is rejected in accordance with our comment in that connection.

(R–94) This involves changes in the list of operating-expense accounts for class A companies appearing at page 64 of the uniform

system to correspond with the following; also the segregation of a portion of maintenance expenses under a new account [601], "Supervision of maintenance"; the classification of the remaining expense included under effective account 602, "Repairs of outside plant", into six new accounts [602a], "Repairs of pole lines," [602b], "Repairs of aerial wire", [602c], "Repairs of aerial cable", [602d], "Repairs of underground conduit", [602e], "Repairs of underground cable", and [602f], "Repairs of submarine cable"; and the exclusion from the maintenance-expense group of accounts 608, "Depreciation", and 609, "Extraordinary retirements". The last point is correlated with recommendation R–95 and is covered by our comment thereunder.

We regard the segregation of cost of supervision as undesirable, because it would impair the completeness of the other maintenance-expense accounts. The proposed requirement that repairs of outside plant be analyzed and accounted for in accordance with types of plant would involve practical difficulties and expense tending to outweigh any probable advantage. In any event the object sought by the recommendation in these respects may be accomplished by those commissions having jurisdiction through the requirement of subdivision.

(R–95) Proposes the creation of a new subdivision of operating-expense accounts for class A and class B companies under the heading of "Depreciation and amortization", to follow the maintenance group and to consist of account 608, "Depreciation", and 609, "Extraordinary retirements," from that group, together with proposed account [613], "Amortization of intangible property". In view of our disapproval under R–100 of the proposal to create the last-mentioned account it is possible that the present recommendation would not be pressed. We shall, however, discuss it briefly.

No special necessity or substantial reason for the proposed refinement in classification is advanced. In the absence thereof there appears to be enough in common between the expense of depreciation and extraordinary retirements, and that of maintenance, to warrant their being classified together even assuming that a line of demarcation could be definitely drawn. In fact, however, under the system of units and depreciation accounting prescribed by the uniform system there is inevitable overlap among these items so that without including charges for depreciation and extraordinary retirements the total expense of maintenance would be understated.

(R–96) This recommendation involves merely the change of title of account 672, "Relief and pensions", in the list of operating-expense accounts appearing on page 65 of the uniform system in conformity with a proposal to that effect which is rejected hereinafter under R–107.

(R–97) This involves an amendment to the text of paragraph (B) of account 605, "Repairs of station equipment", identical with that considered under R–32, and the adverse disposition there made is applicable here.

(R–98) This involves a revision of the text of account 608, "Depreciation", in order to correlate its scope with the proposed amendment of instruction 81, "Depreciation charges", which was disposed of adversely under R–35 in accordance with the rejection under R–116 of the proposal to allocate a portion of the charges for depreciation to account 704, "Supply expense".

(R–99) Involves amendments of the text of account 609, "Extraordinary retirements", which are entirely correlated with those considered under R–59 and therefore covered by our adverse decision in that connection.

(R–100) Under this recommendation it is proposed to create a new operating-expense account [613], "Amortization of intangible property", for the inclusion of charges necessary to amortize leaseholds, limited-term franchises, patents, and similar intangible property included in the plant accounts. This would result in grouping charges separately covered by the following provisions of the uniform system respectively; paragraph (C) of account 671, "Operating rents", paragraph (B) of accounts 673, "Telephone franchise requirements", paragraph (B) of account 675, "Other expenses", and paragraph (A) of the last-mentioned account.

Our attention has not been directed to any advantage which would result from the proposed method of accounting, nor is any apparent, except that of affording a ready means of arriving at particular totals. If this is the result desired, it could be effectually accomplished by subdivision of the accounts now prescribed. The present classification is based upon the character of the several items and appears to be warranted by the analogies existing between the amortization charges for which provision is made and certain of the current expenditures covered by the respective accounts above mentioned.

The text of the proposed new account would further require that adjustments for profit or loss on retirement of intangible property of the nature in question be included therein instead of being made through surplus as at present provided. In our comment under R–73 we held against the adoption of the principle involved herein.

(R–101) This is a recommendation to eliminate account 611, "Employment stabilization", which provides for the inclusion of amounts systematically accrued for maintenance to be performed in accordance with an employment stabilization program designed to

spread the total volume of maintenance work more evenly from year to year. In the alternative it is recommended that the text of paragraph (A) be so amended as to condition charges to this account upon approval, both by ourselves as now provided and by the State commission having jurisdiction, of the company's program, etc. The latter would involve the unauthorized surrender of power to the State commissions.

While possibly in the nature of an advance step, this account is designed to provide, under proper safeguards, the accounting means for dealing with a problem the importance of which is emphasized by present economic conditions. Whether it will prove to be a source of benefit or abuse is difficult to say, but we are in a position to control the use of this account and observe how it is administered. We are not persuaded that it should be withdrawn.

(R–102) These recommendations are directed to the elimination of the fifth item in the list following the text of account 661, "Executive department", and the note thereto referring to account 323, "Miscellaneous income charges", also the corresponding items and notes to accounts 662, "Accounting department", 663, "Treasury department", and 664, "Law department". The items call for the inclusion, in the respective accounts, of membership fees and dues in associations, and the notes direct attention to the fact that such charges must pertain to associations directly or intimately related to telephone operations.

These recommendations are rejected in accordance with our decisions under R–89.

(R–103) Proposes substituting reference to account [134.1], "Capital stock expense", instead of the reference to account 201 made in note B to account 663, "Treasury department", dealing with the cost of printing certificates of original and additional issues of capital stock.

In view of our disposition under R–58 of the proposal to create a new account [134.1], "Capital stock expense", this recommendation is rejected.

(R–104) Proposes amendment of the eleventh item in the list following the text of account 664, "Law department", so as to eliminate therefrom law expenses in connection with rate cases. Would also add to note B a parenthetical reference to proposed account 670, "Regulatory commission expenses".

This proposal is made for the purpose of coordination with recommendation R–105 and is sufficiently covered in the discussion of the latter.

(R–105) Involves creating a new operating-expense account for the inclusion of expenses connected with formal cases before regu-

latory commissions or [and] cases in which such commission is a party.

When this matter was first mentioned at the hearing the point was made that the uniform system includes expenses of this kind under account 664, "Law department", account 675, "Other expenses", and many other accounts. Presumably treatment in the nature of cost accounting was desired for the purpose, among others, of spreading these items over a period of years. But the proposed text thereafter submitted does not measure up to the requirements of cost accounting, in that substantial portions of the costs indicated by the title are not covered. While there is some ambiguity in the statement of the first group of items under paragraph (B), presumably, even though regular employees of the character enumerated usually devote some of their time to work of the nature specified, no part of their compensation is includible unless they are specially assigned thereto. This construction is fortified by a consideration of the statement of the second and third groups of items.

Furthermore, considerable portions of the time of general officers and employees are consumed in preparing and attending the presentation of matters before regulatory commissions, whereas none of this seems to be comprehended by the proposed text. On the other hand, to carve out from the other accounts all the items involved and prescribe the necessary apportionment of the compensation of officers and employees, would result in undesirable fluctuation in other accounts.

The second sentence of the text of paragraph (A) is in conflict with our ruling in case 72, accounting bulletin 11, wherein we held that the proportion of the expenses of a utilities commission borne by a company is chargeable as taxes which, under the uniform system, are includible in account 305, "Operating taxes".

The wording of the note would exclude from the proposed account expenses incurred in rendering special reports ordered to be furnished in cases of the character embraced in the text, whereas it was presumably intended to apply only to reports regularly furnished in response to continuing orders.

For the above reasons the recommendation cannot be adopted as made, but in view of the probable statistical value of information of the character in question we have incorporated a schedule in our forms for annual reports of class A telephone companies, under which regulatory commission expenses are to be shown.

(R–106) This involves the elimination of paragraph (C) of account 671, "Operating rents", in harmony with the proposal to include

charges on account of amortization of leaseholds in a new account [613], "Amortization of intangible property", and is rejected in accordance with our comment under R–100.

(R–107) Under this recommendation it is proposed to change the title of account 672, "Relief and pensions", to "Employees' pensions and benefits".

The text of this account embraces pensions and other benefits paid to active and retired employees, their representatives or beneficiaries, etc. It would appear, therefore, that if the proposed substitute embodies additional significance, it nevertheless sacrifices technical accuracy in the unqualified use of the term "employees." In our opinion any ineptitude in the effective title is not of such serious character as to warrant the substitution.

It is proposed to amend paragraph (D) so as to condition the adoption of the accrual plan of accounting for pensions upon the furnishing of the details thereof to any State commission having jurisdiction as well as to ourselves, as now provided. Inasmuch as the views of the State commission might well be helpful to us this proposal is approved. Accordingly the paragraph will be revised to read as follows:

(D) Before adopting the accrual plan of accounting for pensions the company shall inform any State commission having jurisdiction and this Commission of the details of its pension plan giving full statement of the facts which in its judgment established a contractual obligation for pension payments together with the actuarial formula under which it proposes to create its pension trust fund, and also a copy of the declaration of trust under which the fund is established.

It is also proposed to eliminate paragraph (F), which provides for including in a subaccount accruals for payment of termination allowances to employees and for proper relief to former employees, or alternatively to condition the making of charges to such subaccount upon approval of any State commission having jurisdiction as well as that of this Commission, as presently provided. The latter involves unauthorized surrender of power to the State commissions. With respect to the first alternative, the provision in question was promulgated in recognition of the fact that some telephone companies have been making payments of the nature above mentioned, and the record furnishes no adequate, if any, reason for withdrawing it.

It is further proposed to subjoin a new paragraph (G) requiring the entry of credits in this account representing the portion of each class of benefits attributable to construction, plant removal, and custom-work labor. So far as the first of these classifications is con-

cerned, the proposal has been disposed of under R–18. Furthermore, for reasons indicated in that connection, we think that with respect to the remaining classifications the recommendation would involve undue refinement in accounting.

(R–108) This involves the elimination of paragraph (B) of account 673, "Telephone franchise requirements", in harmony with the proposal to include charges on account of amortization of limited-term franchises in a new account [613], "Amortization of intangible property", and is rejected in accordance with our comment under R–100.

(R–109) This involves eliminating paragraph (B) of account 675, "Other expenses", together with the related words "Amortization of patents" appearing in the first item listed thereunder, in harmony with the proposal to include charges on account of amortization of patents in a new account [613], "Amortization of intangible property". The point is covered by our comment under R–100.

It is also proposed to restrict the above-mentioned first item to amounts paid for patents having an estimated service life of one year or less, and patents acquired at small cost, thereby eliminating reference to patents acquired in an undeveloped state and patents of doubtful service value. The result would be that the cost of patents in the latter group having a life exceeding one year would be chargeable to account 203, "Patent rights".

The reason assigned in support of the proposal is that charges of the nature under discussion should be kept in suspense pending a determination of their character. It may be that this procedure would be proper if necessary. If the point made goes beyond the difficulty of application and into the substance of the present classification, it may be said that patents acquired in an undeveloped state should not be capitalized because the cost thereof is likely to represent but a small fraction of the ultimate cost of development. Moreover, it would seem that a proposal to capitalize patents of doubtful service value carries its own refutation. We are of the opinion that the recommendation should not be adopted.

(R–110) (R–113) These recommendations are directed to the elimination of the fourth item in the list following the text of account 675, "Other expenses", calling for the inclusion of contributions directly or intimately related to the protection of the property of the company, etc., also note D to said account directing attention to the fact that in the absence of such relation contributions shall be charged to account 413, "Miscellaneous debits to surplus."

These recommendations are rejected in accordance with our decision under R–91.

(R–111) Would amend account 675, "Other expenses", by eliminating the last item in the list following the text thereof so as to exclude losses of current funds due to bank failures.

This proposal is correlated with recommendation R–92 whereunder it is proposed to charge to account 413, "Miscellaneous debits to surplus", losses of any funds arising in the manner mentioned. The effective provision recognizes the principle that the loss of funds kept on deposit in banks as a necessary incident of operation constitutes an operating expense. This is in accordance with our ruling in case 94, accounting bulletin 11. For accounting purposes the presumption would be that current funds are held for operating purposes. Of course, the facts developed in a particular investigation might rebut this presumption as to part or all of the funds and call for other treatment. Without prejudice to any such determination in a proper case, the recommendation is rejected.

(R–112) Proposes inserting in the list following the text of account 675, "Other expenses", an item calling for the inclusion of membership fees and dues of the company in associations of telephone companies and of employees in professional organizations.

This recommendation is correlated with the matter discussed under R–89 and is rejected in accordance with our decision in that connection.

(R–114) Involves amendment of parenthetical clause following note C, and the sixth item following the text of account 675, "Other expenses", correlating with proposed account 670 "Regulatory commission expenses". The former would merely add a cross-reference. The latter would call for the inclusion in account 675 of costs of valuations, inventories, and appraisals taken in compliance with orders of regulatory authorities not covered by proposed account 670, unless excluded from the first-mentioned account in accordance with notes B and C thereto.

These proposals are rejected in accordance with our decision under R–105.

(R–115) Under this recommendation there would be added to the text of paragraph (A) of account 702, "Vehicle and other work equipment expense", a provision expressly excluding depreciation on equipment of storerooms. This provision could be treated as incident to the proposal to include such charges under account 704, which is rejected in our comment under R–116. Conceivably, however, it might be based on independent considerations and thus merit further discussion.

It is true that in specifying the inclusion of depreciation charges on plant classified under account 264, "Vehicles and other work

equipment", there is no intention to cover what is essentially equipment of storerooms, and primarily includible under account 261, "Furniture and office equipment". Nevertheless, as a result of marginal instances and practical considerations arising in classification, some portion of equipment of storerooms might incidentally be lodged in account 264. In such event, it would be an undue refinement to require subdivision of the latter for the purpose in question. As the recommendation might be supposed to require this, we think it should be rejected.

(R–116) This would amend the text of paragraph (A) of account 704, "Supply expense", by adding a provision requiring the inclusion of depreciation on equipment of storerooms. As this kind of property is primarily includible in account 261, "Furniture and office equipment", provision is now made for depreciation thereon through charges to account 608, "Depreciation". The recommendation would, therefore, involve subdividing account 261. Storeroom equipment is used primarily for maintenance purposes and since the investment therein is relatively small, the portion of depreciation thereon which might theoretically be chargeable to plant accounts is not a matter of consequence. In our opinion the recommendation involves a refinement of accounting which is not warranted.

(R–117) To the extent that they appear to be material, the proposed amendments of the text of paragraph (B) of account 705, "Engineering expense", involve the introduction of *expense* in addition to time as the basis of apportionment to the appropriate accounts, and the elimination of the alternative of apportioning on such equitable basis as may be fixed by the officers of the company.

The first proposal conflicts with both the effective and proposed provisions with respect to apportionment on the basis of *service* rendered. Furthermore, the items of expense allocable to particular jobs would ordinarily be relatively small, so that to include them in the basis of apportionment would involve undue refinement even if they could be said to be representative.

The alternative method was provided in recognition of the fact that the time basis might in some instances be unduly rigid and that further study might develop a method of apportionment that would be more logical and satisfactory for general application. We deem it inadvisable to withdraw this provision.

The further proposal to add a new paragraph (C), which would require that expenses incurred in connection with projects not carried out be charged to account 418, "Miscellaneous debits to surplus", is unnecessary in view of the provisions of account 139, "Other deferred debits". The uniform system contemplates that clearing accounts will be cleared currently so far as practicable. Engineering

expenses relating to projects under contemplation should be cleared to accounts whose balances are includible in account 139, and the text of the latter expressly provides that preliminary costs in respect of contemplated projects subsequently abandoned shall be charged to account 413.

(R–118) Involves amendments of that portion of the text of paragraph (B) of account 706, "Plant supervision expense", relating to plant engineering, similar to those considered under R–117 in connection with the corresponding paragraph of account 705, with the added condition that the revised basis would be subject to replacement by another basis at the order of the State commission having jurisdiction. The latter provision, as heretofore observed, would involve an unauthorized delegation of power to the State commissions.

It is further proposed to amend the note to this account, which provides for the exclusion of pay and expenses of certain foremen and other supervisory employees except those engaged in the general supervision of maintenance and construction work, by expressly covering plant removals in the last clause in addition to maintenance and construction. This is presumably correlated with the proposal to classify the expense of depreciation and extraordinary retirements separately from maintenance, which was disposed of adversely under R–95. Since the term "maintenance" as here used includes plant removals, the recommendation is rejected.

Conclusions.—We conclude that the Uniform System of Accounts for Telephone Companies, First Revised Issue, should not be rescinded, but that it should be further revised as specified in the foregoing statement; that in view of the nature and limited scope of such further revisions, that portion of the order of December 27, 1932, herein, which provided that they should become effective as of January 1, 1933, should not be vacated; that said uniform system as thus revised should be made effective as of January 1, 1933, and January 1, 1934, for class A and class B telephone companies, respectively; and that all class A telephone companies and all class B telephone companies that elected to adopt the uniform system as of January 1, 1933, should be required to restate their accounts for the years 1933 and 1934 in accordance therewith as thus revised.

FARRELL, *Commissioner*, dissenting:

I do not concur in the issuance of this report, because I believe the expense connected with its publication to be unjustifiable. The telephone companies cannot be required to comply with the findings in the report except through the issuance of an order, and such an order, issued by the Interstate Commerce Commission, cannot be

made effective inside of 30 days from the date of its issuance. Long before the expiration of that period of time the Federal Communications Commission will have been organized and the law under which such a report and order can now be made will have become a thing of the past. In other words, any change in the accounting rules for telephone companies hereafter required by a Federal regulating tribunal to be made will necessarily be the result of action to be taken by the Federal Communications Commission under the Communications Act of 1934, approved June 19, 1934.

Am authorized to state that COMMISSIONER AITCHISON concurs in this expression.

COMMISSIONER EASTMAN participated in the disposition of this case.

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EXHIBIT B OF PLAINTIFFS' BILL OF COMPLAINT.

Uniform System of Accounts

for

Telephone Companies

PRESCRIBED BY THE

FEDERAL COMMUNICATIONS COMMISSION

IN ACCORDANCE WITH THE PROVISIONS OF THE
COMMUNICATIONS ACT OF 1934

Issue of June 19, 1935
Effective January 1, 1936

UNITED STATES
GOVERNMENT PRINTING OFFICE
WASHINGTON : 1935

For sale by the Superintendent of Documents, Washington, D. C - - Price 15 cents

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TELEPHONE DIVISION ORDER NO. 7–C

Commissioners Walker, *Chairman*, Brown, and Prall:

In a regular meeting of the Telephone Division of the Federal Communications Commission, held on the nineteenth day of June, 1935:

Whereas under our Order No. 7, it was ordered that representatives of the several States and of the commissions or regulatory bodies thereof having jurisdiction over telephone carriers therein, and all other parties at interest, should have until October 1, 1934, within which to file exceptions or objections to the report of the Interstate Commerce Commission, rendered in its Docket No. 25705, affecting accounting rules for telephone companies, or to suggest amendments or changes in such accounting rules for telephone companies; and that all exceptions, objections, and suggestions should be filed in writing and 15 copies thereof provided within the time therein specified;

Whereas under our Order No. 7–A, it was ordered that an extension of time be granted to November 1, 1934, for the filing of such exceptions, objections, or suggested amendments; and that Order No. 7 be set down for hearing and oral argument by the parties on November 16, 1934, before the Telephone Division in its hearing room at Washington, D. C.;

Whereas certain exceptions or objections to the report of the Interstate Commerce Commission rendered in its Docket No. 25705, and certain suggested amendments or changes in such accounting rules, were filed pursuant to said Orders No. 7 and No. 7–A, by parties at interest;

Whereas a hearing was held and arguments were heard pursuant to said orders, which said orders are hereby referred to and made a part hereof;

Whereas a draft of a Uniform System of Accounts for Telephone Companies, known as "Issue Effective Janu-

ary 1, 1936", was adopted by the Telephone Division by its Order No. 7–B of May 1, 1935, which said draft and order were submitted to all parties in interest;

Whereas by notice issued on May 1, 1935, the Telephone Division announced that telephone carriers and other interested parties might file exceptions to such accounting rules on or before May 16, 1935, and by the same notice announced a conference with State commission representatives and representatives of the telephone carriers on May 16, 1935, for the consideration of any exceptions filed; and

Whereas exceptions were filed and such conference was held:

Now therefore, after hearing the evidence and arguments and having held the conference, and being fully advised in the premises and pursuant to its findings, the Telephone Division does make the following orders, to wit:

It is ordered, That Order No. 7–B, together with the draft of the Uniform System of Accounts for Telephone Companies, known as "Issue Effective January 1, 1936", and promulgated on May 1, 1935, be, and the same is hereby, superseded by this Order No. 7–C, and by a Uniform System of Accounts for Telephone Companies, hereafter called "Issue of June 19, 1935, Effective January 1, 1936."

It is further ordered; That the report of the Interstate Commerce Commission in its Docket No. 25705 affecting accounting rules for telephone companies and the Uniform System of Accounts for Telephone Companies prescribed for the use of telephone companies by Division 4 of the Interstate Commerce Commission on the 12th day of November 1932, and known as "First Revised Issue", be amended or changed; that said "First Revised Issue", as amended or changed shall be embodied in printed form to be hereafter known as "Issue of June 19, 1935, Effective January 1, 1936", a copy of which is now before this Commission, and is hereby approved; that a copy thereof duly authenticated by the Secretary of the Commission be filed

in its archives, and a second copy thereof, authenticated in like manner, in the office of the Accounting, Statistical, and Tariff Department; and that each of said copies so authenticated and filed shall be deemed an original record thereof.

It is further ordered, That the Uniform System of Accounts for Telephone Companies embodied in said "Issue of June 19, 1935, Effective January 1, 1936" be, and the same is hereby, prescribed for the use of telephone companies having average annual operating revenues exceeding $50,000, subject to the provisions of the Communications Act of 1934, in the keeping and recording of their accounts; that each and every such carrier and each and every receiver or operating trustee of any such carrier be required to keep all accounts in conformity therewith; and that a copy of said "Issue of June 19, 1935, Effective January 1, 1936" be sent to each and every such carrier and to each and every receiver or operating trustee of any such carrier.

It is further ordered, That in order that the basis of comparison with previous years be not destroyed, each and every such carrier and each and every receiver or operating trustee of any such carrier shall, during the 12 months from the time that the said "Issue of June 19, 1935, Effective January 1, 1936" becomes effective, keep and maintain, in addition to the accounts hereby prescribed, such portion or portions of its present accounts as may be necessary for the purpose of such comparison; and during the same period, shall maintain such groupings of the primary accounts hereby prescribed as may be necessary for that purpose.

It is further ordered, That nothing herein contained shall be construed as prohibiting or excusing any such carrier or receiver or operating trustee of any such carrier, from subdividing the accounts hereby prescribed in the manner ordered by any State commission having jurisdiction or to the extent necessary to secure the information required in the prescribed reports to such commission.

It is further ordered, That said "First Revised Issue" prescribed by Division 4 of the Interstate Commerce Commission, as aforesaid, shall remain in full force and effect up to and including the 31st day of December 1935, and that said "Issue of June 19, 1935, Effective January 1, 1936" herein prescribed, as aforesaid, shall become effective on the 1st day of January 1936.

By the Commission, Telephone Division:

[SEAL] HERBERT L. PETTEY,
Secretary.

INTRODUCTORY LETTER

FEDERAL COMMUNICATIONS COMMISSION,
Washington, D. C., June 19, 1935.

TO TELEPHONE COMPANIES:

In accordance with the order of the Federal Communications Commission, the text of which immediately precedes this letter, this Uniform System of Accounts for Telephone Companies will supersede, on January 1, 1936, the Uniform System of Accounts for Telephone Companies, First Revised Issue, prescribed by the Interstate Commerce Commission.

As stated in the preceding order, this Uniform System of Accounts for Telephone Companies is prescribed for the use of telephone companies subject to the act having average annual operating revenues exceeding $50,000. No uniform system of accounts has been prescribed for the use of telephone companies having average annual operating revenues not exceeding $50,000.

Attention is directed to section 220 (d) of the act which provides as follows:

> In case of failure or refusal on the part of any such carrier to keep such accounts, records, and memoranda on the books and in the manner prescribed by the Commission, or to submit such accounts, records, memoranda, documents, papers, and correspondence as are kept to the inspection of the Commission or any of its authorized agents, such carrier shall forfeit to the United States the sum of $500 for each day of the continuance of each such offense.

Acknowledgment is hereby made of the value of the report of the Interstate Commerce Commission in its Docket No. 25705, Accounting Rules for Telephone Companies. In that report objections to the Uniform Sys-

tem of Accounts for Telephone Companies, promulgated by the Interstate Commerce Commission on November 12, 1932, were considered. The findings of that Commission in its report were very helpful to this Commission in the preparation of this Uniform System of Accounts.

PAUL A. WALKER,
Chairman, Telephone Division.

INSTRUCTIONS

General

1. **Classification of companies.**—(A) For the purpose of this system of accounts, telephone companies are divided into two classes as follows:

Class A.—Companies having average annual operating revenues exceeding $100,000.

Class B.—Companies having average annual operating revenues exceeding $50,000, but not more than $100,000.

(B) Class A companies shall keep all the accounts of this system of accounts, which are applicable to their affairs.

(C) Class B companies shall keep all the accounts of this system of accounts, which are applicable to their affairs, except that their accounts for operating revenues and operating expenses may be kept under the accounts of the condensed classification provided for herein.

(D) No uniform system of accounts has been prescribed for companies having average annual operating revenues not exceeding $50,000.

NOTE.—In order that frequent changes may be avoided, companies operating established telephone plants shall adopt the scheme of accounts indicated by the average of their annual revenues for 3 years immediately preceding the effective date of this order. If at the close of any calendar year the average of the annual revenues for the 3 latest years is greater than the amount applicable to the class in which the company has been accounting, the higher scheme of accounts shall be adopted. New companies shall estimate the amount of their annual revenues and adopt the scheme of accounts appropriate for the amount of such estimated revenues.

2. **Records.**—(A) The company's records shall be kept with sufficient particularity to show fully the facts pertaining to all entries in these accounts. Where the full information is not recorded in the general books the entries therein shall be supported by other records in which the full details shall be shown and the general book entries shall contain sufficient reference to the detail records to permit ready identification. The detail records shall be filed in such manner as to be readily accessible for examination by representatives of this Commission.

(B) Attention is directed to the following extract from section 220 of the Communications Act of 1934:

"(e) Any person who shall willfully make any false entry in the accounts of any book of accounts or in any record or memo-

randa kept by any such carrier, or who shall willfully destroy, mutilate, alter, or by any other means or device falsify any such account, record, or memoranda, or who shall willfully neglect or fail to make full, true, and correct entries in such accounts, records, or memoranda of all facts and transactions appertaining to the business of the carrier, shall be deemed guilty of a misdemeanor, and shall be subject, upon conviction, to a fine of not less than $1,000 nor more than $5,000 or imprisonment for a term of not less than one year nor more than three years, or both such fine and imprisonment: *Provided*, That the Commission may in its discretion issue orders specifying such operating, accounting, or financial papers, records, books, blanks, or documents which may, after a reasonable time, be destroyed, and prescribing the length of time such books, papers, or documents shall be preserved."

The Interstate Commerce Commission's order specifying records which may be destroyed is contained in its "Regulations to Govern the Destruction of Records of Telephone, Telegraph, and Cable Companies, Issue of 1920", which order remains in effect, except as hereinafter modified and except as further provided by Telephone Division Order No. 6–A, dated December 20, 1934.

(B. 1) All charges to the accounts prescribed in this classification for telephone plant, income, operating revenues, and operating expenses shall be just and reasonable and any payments by the company in excess of such just and reasonable charges shall be included in account 323, "Miscellaneous income charges."

(C) Accounts which are clearly summaries of other accounts or subaccounts provided for herein are not required to be kept in the company's books. All accounts kept shall conform in numbers and titles to those prescribed herein, except that:

(1) Companies may subdivide any of the accounts, provided such subdivisions do not impair the integrity of the accounts prescribed. The titles of all such subdivisions or subaccounts shall refer by number or title to the accounts of which they are subdivisions, and this Commission shall be notified of the nature and purpose of such subdivisions. When subaccounts are thus kept, it is not required that the main accounts of which they are subdivisions shall also be kept in the company's books.

(2) Clearing accounts, in addition to those prescribed herein, may be kept when necessary in making the proper distribution of items to the appropriate primary accounts, provided that within 30 days of the opening of such accounts, this Commission shall be notified of the nature and purpose thereof.

(3) Temporary or experimental accounts may be kept in addition to the accounts prescribed herein, for the purpose of developing the efficiency of operations, etc., provided such accounts do not impair the integrity of any accounts prescribed herein, and pro-

vided further that within 30 days of the opening of such accounts, this Commission shall be notified of the nature and purpose thereof.

(D) As of the effective date of this system of accounts, the several accounts prescribed herein shall be opened by transferring thereto the balances carried in the accounts previously maintained by the company. Copies of the journal entries recorded to effect these transfers shall be filed with this Commission. The company is authorized to make such subdivisions, reclassifications, or consolidations of such balances as are necessary to meet the requirements of this system of accounts.

3. **Definitions.**—When used in this system of accounts:

(A) "Accounts" or "These accounts" means the accounts of this system of accounts.

(B) "Actually issued", as applied to securities issued or assumed by the company, means those which have been sold to bona fide purchasers for a valuable consideration (including those issued in exchange for other securities or other property) under the condition that the purchasers secured them free from all control by the issuing company, also securities issued as dividends on stock.

(C) "Actually outstanding", as applied to securities, means those which have been actually issued and are neither retired nor held by or for the company.

(D) "Affiliated companies" means companies that directly or indirectly through one or more intermediaries, control or are controlled by, or are under common control with, the accounting company.

"Control" (including the terms "controlling", "controlled by", and "under common control with") means the possession, directly or indirectly of the power to direct or cause the direction of the management and policies of a company, whether such power is exercised through one or more intermediary companies, or alone, or in conjunction with, or pursuant to an agreement with, one or more other companies, and whether such power is established through a majority or minority ownership or voting of securities, common directors, officers, or stockholders, voting trusts, holding trusts, affiliated companies, contract, or any other direct or indirect means.

(D.1) "Book amount", as applied to capital stock, means the par value of stock having a par value, and the amount duly authorized for inclusion in account 150, "Capital stock", for stock having no par value.

(E) "Book cost" means the amount at which property is recorded in these accounts, without deduction of related reserves.

(F) "Book liability" means the amount at which securities issued or assumed by the company and other liability items are recorded in these accounts.

(G) "Company" or "The company", when not otherwise indicated in the context, means the accounting company.

(G.1) "Cost", except as applied to telephone plant, franchises, patent rights, and right-of-way, means the amount of money actually paid (or the current money value of any consideration other than money exchanged) for property or services. (Note also instruction 3–S.1.)

(H) "Cost of removal" means the cost of demolishing, dismantling, removing, tearing down, or otherwise disposing of telephone plant and recovering the salvage, including the cost of transportation and handling incident thereto.

(I) "Debt expense" means all expenses in connection with the issuance and sale of evidences of debt, such as fees for drafting mortgages and trust deeds; fees and taxes for issuing or recording evidences of debt; cost of engraving and printing bonds, certificates of indebtedness, and other commercial paper; fees paid trustees; specific costs of obtaining governmental authority; fees for legal services; fees and commissions paid underwriters, brokers, and salesmen; fees and expenses of listing on exchanges, and other like costs. (Note also instruction 13–B.)

(J) "Depreciation", as applied to depreciable telephone plant, means the loss in service value (note instruction 3–Y) not restored by current maintenance, incurred in connection with the consumption or prospective retirement of telephone plant in the course of service from causes which are known to be in current operation, against which the company is not protected by insurance, and the effect of which can be forecast with a reasonable approach to accuracy. Among the causes to be given consideration are wear and tear, decay, action of the elements, inadequacy, obsolescence, changes in the art, changes in demand and requirements of public authorities.

(K) "Discount", as applied to securities issued or assumed by the company, means the excess of the book or face amount (note instruction 3–D.1–K.1) of the securities plus interest or dividends accrued at the date of the sale over the current money value of the consideration received at their sale.

(K. 1) "Face amount" means the amount or "value" of bonds, mortgages, and other evidences of debt set forth in the documents themselves.

(L) "Group plan", as applied to depreciation accounting, means the plan under which depreciation charges are accrued upon the basis of the original cost (note instruction 3–S.1) of all property included in each depreciable plant account, using the average service life thereof properly weighted, and upon the retirement of any depreciable property its full service value is charged to the depreciation reserve whether or not the particular item has attained the average service life.

(M) "Investment advances", means advances, represented by notes or by book accounts only, with respect to which it is mutually agreed or intended between the creditor and the debtor that they shall be settled by the issuance of capital stock or funded debt or shall not be subject to current cash settlement.

(N) "Minor items", as applied to depreciable telephone plant, means any part or element which is not designated as a unit of property in Appendix A.

(O) "Miscellaneous physical property" means all physical property owned by the company, other than telephone property the investment in which is includible in accounts 100.1, "Telephone plant in service", 100.2, "Telephone plant under construction", and 100.3, "Property held for future telephone use."

(P) "Net salvage value" means the salvage value (note instruction 3–W) of the property retired after deducting the cost of removal.

(Q) "Nominally issued", as applied to securities, means those which have been signed, certified, or otherwise executed and placed with the proper officer for sale, or pledged or otherwise placed in some special fund of the company, but which have not been sold.

(R) "Nominally outstanding", as applied to securities, means those which after being actually issued have been reacquired by or for the company under such circumstances as require them to be considered as held alive and not retired.

(S) "Nonaffiliated companies" means all companies other than those defined as affiliated in instruction 3–D.

(S.1) "Original cost" or "Cost", as applied to telephone plant, franchises, patent rights, and right-of-way, means the actual money cost of (or the current money value of any consideration other than money exchanged for) property at the time when it was first dedicated to the public use, whether by the accounting company or by a predecessor public utility. (Note also instruction 3–G.1.)

(T) "Plant retired" means plant which has been removed, sold, abandoned, destroyed, or otherwise withdrawn from telephone service.

(U) "Premium", as applied to securities issued or assumed by the company, means the excess of the current money value of the consideration received at their sale over the sum of their book or face amount (note instruction 3–D.1–K.1) and interest or dividends accrued at the date of the sale.

(V) "Replacing" and "replacement", when not otherwise indicated in the context, mean the construction or installation of telephone plant in place of plant retired, together with the removal and recovery of the plant retired.

(W) "Salvage value" means the amount received for property retired, if sold, or if retained for reuse, the amount at which the

material recovered is chargeable to account 122, "Material and supplies."

(X) "Service life" means the period between the time of installation (note instruction 3–CC) of telephone plant and the time of its retirement.

(Y) "Service value" means the difference between the original cost and:

(1) The salvage value (note instruction 3–W) for station apparatus.

(2) The net salvage value (note instruction 3–P) for other telephone plant.

(Y.1) "Stock expense", as applied to capital stock, means all expenses in connection with the issuance, sale, or resale of capital stock, such as fees and commissions (including the cash value of securities) paid to promoters, underwriters, brokers, and salesmen; fees for legal services; cost of soliciting subscriptions for capital stock, including fees, commissions, and advertising; cost of obtaining governmental authority and filing notices thereunder; fees and taxes for issuance of capital stock and listing on exchanges; cost of preparing, engraving, printing, issuing, and distributing prospectuses and stock certificates in connection with both original and additional capital stock issues. (Note also instruction 13–B.)

(Z) "Straight-line method", as applied to depreciation accounting, means the plan under which the service value (note instruction 3–Y) of property is charged to operating expenses and to clearing accounts and credited to the depreciation reserve through equal annual charges as nearly as may be during its service life.

(AA) "Telephone operations" and "telephone service" mean the service by common carriers of transmitting intelligence by wire or wireless primarily through the use of telephones, and services incidental or auxiliary to such service, such as private line, teletypewriter, telegraph, and telephotograph services.

(BB) "Telephone plant" means physical property used in telephone service.

(CC) "Time of installation" means the date at which telephone plant is completed ready for service.

(DD) "Time of retirement" means the date at which telephone plant is retired from telephone service.

4. **Unaudited items.**—When the amount of any known item affecting these accounts cannot be accurately determined in time for inclusion in the accounts of the calendar year in which the transaction occurs, the amount of the item shall be estimated and included in the proper accounts. When the item is audited, the necessary adjustments shall be made through the accounts in which the estimate was recorded. If during the interval between

the date of inclusion of the item in the accounts and the date on which it is audited, a substantial difference from the initial estimate is determined, appropriate adjustments shall be made in the current accounts to cover such difference. The company is not required to anticipate minor items which would not appreciably affect these accounts.

5. **Delayed items.**—(A) The term "delayed items" means items relating to transactions which occurred before the current calendar year. It includes adjustments of errors in the income, operating revenue, and operating expense accounts of prior years.

(B) If the amount of any delayed item is relatively so large that its inclusion in the accounts for a single year would seriously distort those accounts, the company shall distribute to surplus so much of the amount as affects the operations of prior years. The company shall file with this Commission the full particulars concerning each such item, including the accounts and years which would have been affected had the item not been delayed.

6. **Spreading of income, revenue, and expense items.**—When the amount of any unusual item includible in an income, operating revenue, or operating expense account for a single month is relatively so large that its inclusion in the accounts for that month would seriously distort those accounts, it may be included in account 139, "Other deferred charges", or account 174, "Other deferred credits", as appropriate, and distributed in equal amounts to the accounts for the current and remaining months of the calendar year.

7. **Profits and losses from foreign exchange.**—(A) Profits and losses from premiums and discounts on foreign exchange shall be included, so far as practicable, in the accounts appropriate for the transactions in connection with which such items arise. For example, profits realized and losses suffered due to the difference in rates of exchange between the date that money is borrowed or loaned and the date of payment or collection shall be included in account 402, "Miscellaneous credits to surplus", or account 413, "Miscellaneous debits to surplus", as may be appropriate.

(B) Minor amounts of profits and losses on foreign exchange arising in the course of the company's telephone operations and impracticable of allocation to each specific transaction involved shall be included in account 526, "Other operating revenues", or account 675, "Other expenses", as may be appropriate.

8. **Interpretation of item lists.**—Lists of "items" appearing in the texts of the several accounts are given for the purpose of clearly indicating the application of the prescribed accounting in specific cases. The lists are not to be considered as comprising all the items includible in the several accounts but merely as representative of them. On the other hand, the appearance of

an item in a list warrants the inclusion of such item in the account concerned only when the text of the account also indicates inclusion, inasmuch as the same item frequently appears in more than one list. The proper entry in each instance must be determined by the texts of the accounts.

9. Submission of questions.—To the end that uniformity of accounting may be maintained, the company shall submit all questions of doubtful interpretation of the prescribed accounting to this Commission for consideration and decision.

Balance-Sheet Accounts

10. Purpose of balance-sheet accounts.—The balance-sheet accounts (100.1 to 181, inclusive) are designed to show the assets, liabilities, capital stock, and surplus or deficit of the company.

11. Current assets.—(A) In the group of accounts designated as current assets (accounts 113 to 125, inclusive) there shall not be included any item the book cost of which is not reasonably assured, except that items of current character but of doubtful value may be written down and for record purposes carried in these accounts at a nominal amount. If not thus written down, they shall be included in account 139, "Other deferred charges", at book cost or nominal amount, or written off, as may be appropriate; but they shall not be so included at book cost unless there is a reasonable prospect of future substantial value.

(B) The amount of any item written off shall be included in account 530, "Uncollectible operating revenues—Dr.", account 323, "Miscellaneous income charges", account 413, "Miscellaneous debits to surplus", or other appropriate account.

12. Book cost of securities owned.—(A) Securities issued by others shall be recorded in these accounts at the time of purchase at the current money value of the consideration given therefor by the company. (Note also paragraph (D) of account 313 and paragraph (B) of account 314.)

(B) The company is allowed the option of writing down such book cost in recognition of decline in the value of the securities. It shall write down to a nominal amount or write off if there is no reasonable prospect of future substantial value. The amount of such adjustment shall be debited to account 413, "Miscellaneous debits to surplus." The company shall maintain a complete record of the facts on which it bases such adjustment.

13. Company securities owned.—(A) The book or face amount (note instruction 3–D.1–K.1) of nominally issued (note instruction 3–Q) and nominally outstanding (note instruction 3–R) stocks and other securities issued or assumed by the company shall be shown in the short columns only of the balance-sheet statement of the company to this Commission. (Note also instruction 16.1.)

(B) The necessary adjustments for the difference between the face or book amount of securities reacquired and the amounts actually paid for them together with expenses incurred in connection with their reacquisition shall be included, when a debit, in account 413, "Miscellaneous debits to surplus", and when a credit, in account 402, "Miscellaneous credits to surplus."

NOTE.—The book amount for nonpar stock reacquired shall be obtained by first ascertaining the amount in account 150, "Capital stock", for the particular class of stock before the reacquirement. In this amount shall be included the proceeds realized at the sale, the amount of any assessments against stockholders, the amounts transferred to account 150 from surplus, less any amount which has been distributed from account 150 to the stockholders in liquidation. The amount thus ascertained shall be prorated to the shares reacquired on the basis of the proportion that the reacquired shares bear to the total number of shares actually outstanding immediately prior to their reacquirement. (Note also accounts 104, 105, 136, and 137.)

14. Discount and premium on capital stock.—(A) A separate discount and premium account shall be maintained to include both discounts suffered and premiums realized at the time of sale or resale of each class and series of capital stock having a par value. (Note instruction 3–K–U.)

(B) In stating the balance-sheet, the total of debit balances in these accounts having debit balances shall be reported under account 134.1, "Discount on capital stock", and the total of credit balances in these accounts having credit balances shall be reported under account 152, "Premium on capital stock." Accounts with debit balances shall not be offset by accounts with credit balances.

(C) General levies or assessments against stockholders shall be credited to the discount and premium account for the particular class and series of capital stock so assessed.

(D) Discounts, premiums, and assessments on capital stock shall be retained in the discount and premium account until the reacquirement of the securities to which they relate, or until otherwise disposed of lawfully.

(E) When capital stock which has been actually issued or assumed by the company is reacquired, the proportion (based upon the relation of the amount of stock reacquired to the total amount of that particular class or series of stock outstanding before its reacquirement) of the balance in the discount and premium account with respect to the stock reacquired shall be cleared to account 402, "Miscellaneous credits to surplus", or account 413, "Miscellaneous debits to surplus", as may be appropriate.

(F) No discount or premium on capital stock shall be included in any account as a part of the cost of acquiring any property or as a part of the cost of operation.

15. Discount, premium, and expense on long-term debt.—(A) A separate discount, premium, and debt expense account shall be maintained to include both discounts suffered and premiums realized, together with expenses incurred, in connection with the sale or resale of each class and series of long-term debt (including receivers' certificates) issued or assumed by the company. (Note also instructions 3–I–K–U and 13–B.)

(B) In stating the balance-sheet, the total of the debit balances remaining in these accounts having debit balances shall be reported under account 135, "Discount on long-term debt", and the total of credit balances remaining in these accounts having credit balances shall be reported under account 168, "Premium on long-term debt." Accounts with debit balances shall not be offset by accounts with credit balances.

(C) The company may extinguish at any time through charges to account 413, "Miscellaneous debits to surplus", all or any part of the debit balance remaining in any particular discount, premium, and debt expense account.

(D) Each month there shall be credited to each particular discount, premium, and debt expense account in which there is a debit balance the proportion (based upon the ratio of the month to the life of the security remaining at the beginning of the month) of such debit balance as is applicable to the month. The amounts thus credited shall be concurrently charged to account 338, "Amortization of discount on long-term debt." (Note also instruction 22–B–10–b.)

(E) Correspondingly each month there shall be charged to each particular discount, premium, and debt expense account in which there is a credit balance the proportion of such credit balance as is applicable to the month. The amounts thus charged shall be concurrently credited to account 339, "Release of premium on long-term debt—Cr." (Note also instruction 22–B–10–b.)

(F) Except as provided in paragraphs (C), (D), and (E) of this instruction, the balance in each of these accounts shall be carried until the reacquirement of the securities to which it relates, at which time the proportion (based upon the relation of the amount of long-term debt reacquired to the total amount of that particular class or series of long-term debt outstanding before its reacquirement) of the balance in the discount, premium, and debt expense account with respect to the long-term debt reacquired shall be cleared to account 402, "Miscellaneous credits to surplus", or account 413, "Miscellaneous debits to surplus", as may be appropriate. (Note also instruction 13–B.)

(G) No discount, premium, or expense on long-term debt shall be included in any account as a part of the cost of acquiring any property or as a part of the cost of operation except under the provisions of instruction 22–B–10–b.

16. **Exchange of securities.**—Before recording journal entries which it is proposed to spread upon the company's books to record the reacquirement of capital stock or other securities issued or assumed by the company under a plan for the issuance in exchange therefor of the company's securities, a statement indicating the plan of accounting proposed by the company shall be presented to this Commission for consideration and approval. Such statement shall give complete information concerning the plan of exchange; the authority of the regulatory body with respect thereto, if any; and the basis upon which the amounts have been determined.

16.1. **Nonpar capital stock.**—Before recording journal entries which it is proposed to spread upon the company's books to record the issuance or assumption by the company of nonpar capital stock or appropriations of surplus for transfer to nonpar capital stock account, the plan of accounting shall be presented to this Commission for consideration and approval. Such statement shall give complete information with respect to the basis upon which the amounts to be recorded have been determined.

17. **Contingent assets and liabilities.**—Contingent assets represent a possible source of value to the company contingent upon the fulfillment of conditions regarded as uncertain. Contingent liabilities include items which may under certain conditions become obligations of the company but which are neither direct nor assumed liabilities at the date of the balance-sheet. In the annual report to this Commission contingent assets and contingent liabilities shall not be included in the balance-sheet but contingent assets and liabilities shall be shown in detail in a supplementary statement accompanying it.

Telephone Plant Accounts

20. **Purpose of telephone plant accounts.**—(A) The telephone plant accounts (201 to 277, inclusive) are designed to show the original cost (note instruction 3–S.1) of the company's telephone plant (note instruction 3–BB) which ordinarily has a service life of more than 1 year, including such plant whether used by the company or others in telephone service (note instruction 3–AA); also the original cost of franchises, patents, right of way, leaseholds and other interests in land. It shall also include the general expenses of organization of the accounting company.

(B) Telephone plant contributed to the company or constructed by it through expenditures of contributions of money or its equivalent shall be charged to the telephone plant accounts at its original cost (estimated if not known) and there shall be credited to the depreciation reserve and amortization reserve accounts the estimated amounts of the reserve requirements, if any, applicable to

the plant. The difference between the amounts so includible in the telephone plant and the reserve accounts shall be credited to account 175, "Contributions of telephone plant."

NOTE.—Amounts received for construction which are ultimately to be repaid, wholly or in part, shall be credited to account 174; when final determination has been made as to the amount to be returned, any unrefunded amounts shall be credited to account 175.

(C) When telephone plant ordinarily having a service life of more than 1 year is installed for temporary use in telephone service, it shall be accounted for in the same manner as plant having a service life of more than 1 year. This includes temporary installations of station equipment, plant (such as poles, wire, and cable) installed to maintain service during the progress of highway reconstruction or during interruptions due to storms or other casualties, equipment used for the training of operators, equipment used to provide intercepting positions in central offices to handle traffic for a short period following cutover to dial-system service, and similar installations of property for telephone service.

(D) The cost of individual items of equipment, such as tools and office equipment of small value (for example, costing $10 or less) or short life, shall be charged to the appropriate operating expense or clearing accounts according to the use of such items, except that such accounting shall not be permitted when the investment in such property is relatively large and the correctness of the accounting therefor is verified by current inventories.

21. **Telephone plant acquired.**—(A) When property in use in telephone service (note instruction 3–AA) is acquired, the amount of money actually paid (or the current money value of any consideration other than money exchanged) for the property (together with preliminary expenses incurred in connection with the acquisition) shall be charged to account 276, "Telephone plant acquired." (Note also account 139.)

(B) The accounting for the acquisition of the plant shall then be completed as follows:

(1) The original cost, estimated if not known, (note instruction 3–8.1) of telephone plant, governmental franchises and other similar rights acquired shall be charged to the telephone plant accounts, account 100.2, "Telephone plant under construction", and account 100.3, "Property held for future telephone use", as appropriate, and credited to account 276. When the actual original cost cannot be determined and estimates are used, the company shall be prepared to furnish this Commission with the particulars of such estimates.

(2) The amounts of the reserve requirements for depreciation and amortization of the plant acquired shall be credited to account 171, "Depreciation reserve", and account 172, "Amortization reserve", and debited to account 276.

(3) The amount of contributions to the predecessor company or companies for construction and acquisition of the telephone plant acquired shall be credited to account 175, "Contributions of telephone plant", and debited to account 276 on the books of the accounting company.

(4) The amount remaining in account 276, "Telephone plant acquired", applicable to the plant acquired, shall upon completion of the entries provided in the foregoing paragraphs (1), (2), and (3), be debited or credited, as appropriate, to account 100.4, "Telephone plant acquisition adjustment", except that when any amount thus chargeable to account 100.4 applies to duplicate or other telephone plant which will be retired by the vendee in the reconstruction of the acquired property and its consolidation with previously owned property, the accounting for the amount applicable to such plant shall be submitted to this Commission for consideration and approval.

(C) Journal entries recording the acquisition of a complete telephone system, a complete exchange, a complete toll system, or other telephone plant where the consideration paid is $25,000 or more, shall be submitted to this Commission for consideration and approval. The text of such entries shall give a complete description of the property acquired and the bases upon which the amounts of the entries have been determined.

22. Cost of construction.—(A) The cost of construction of property chargeable to the telephone plant accounts shall include the cost of labor, material and supplies, transportation, contract work, relief and pensions, protection, injuries and damages, privileges and permits, taxes, special machine service, interest during construction, insurance, construction services, and other analogous elements in connection with such work.

(B) The following is a description of the major items referred to in the foregoing paragraph:

(1) "Cost of labor" includes the pay and expenses of employees directly engaged in or being trained for construction work, of foremen in direct charge thereof, and an equitable proportion of the cost of local plant administration, general plant supervision and engineering, and of the pay, office, and other expenses of general officers and general office employees devoting part of their time to supervisory, administrative, or clerical functions in connection with construction work.

(2) "Cost of material and supplies" includes the purchase price at the point of free delivery plus the costs of inspection, loading and transportation, and an equitable proportion of supply expense. In determining the cost of material used, proper allowance shall be made for unused material, for material recovered from temporary structures used in performing the work involved, and for discounts allowed and realized in the purchase of material.

(3) "Cost of transportation" includes the cost of transporting employees, material and supplies, tools, and other work equipment. It includes amounts paid therefor to other companies or individuals and the cost of the company's own motor vehicle or other transportation service.

(4) "Cost of contract work" includes amounts paid for work performed under contract by other companies, firms, or individuals, engineering and supervision applicable to such work, costs incident to the award of contracts, and the inspection of such work. The cost of construction work performed by affiliated companies (note instruction 3–D) and other details relating thereto shall be available from the work in progress and supporting records.

(5) "Cost of protection" includes the cost of protecting the company's property from fire or other casualties and the cost of preventing damages to others or the property of others.

(6) "Cost of injuries and damages" includes expenditures or losses in connection with construction work on account of injuries to persons and damages to the property of others. (Note also accounts 669 and 672.)

(7) "Cost of privileges and permits" includes payments for and expenses incurred in securing privileges, permits, or rights in connection with construction work, such as for use of private property, streets, or highways. The cost of such privileges and permits shall be included in the cost of the work for which the privileges or permits are secured, except for costs includible in account 202, "Franchises", and account 207, "Right of way."

(8) "Taxes" includes taxes on physical property during construction and before the facilities are completed ready for service, assessed separately from taxes on operating property or under conditions which permit separate identification or allocation of the amount chargeable to construction.

NOTE.—Taxes on physical property held for future telephone use shall be included in account 100.3.

(9) "Special machine service" includes the cost of labor expended, materials and supplies consumed, and other expenses incurred in the maintenance, operation, and use of special machines, other than transportation equipment, such as steam shovels, pile drivers, etc., and other labor saving machines; also expenditures for rental, maintenance and operation of such machines owned by others. When a construction job requires the purchase of special machines, the cost thereof, less the appraised or salvage value at the time of release from the job, shall be included in the cost of the project.

(10) "Interest during construction" includes the amount of interest upon all moneys, including the company's own funds, used

in the acquisition or construction of telephone property and shall be charged to the accounts appropriate for the cost of the property acquired or constructed as follows:

(a) Reasonable amounts for interest during the construction period (before the property is received or is completed ready for telephone service) on general funds expended for the acquisition or construction of telephone plant shall be charged to the telephone plant accounts and credited to account 313, "Interest income."

(b) When funds, derived from the sale of bonds, notes, and other interest-bearing debt, are specifically acquired and separately held for use in the construction of telephone plant, the total interest, discount or premium, and expense on such debt, less interest earned on such funds, applicable to the accounting period shall be included in the cost of telephone plant and credited to account 313, "Interest income", provided, however, that no interest charge for a longer period than 6 months prior to the commencement of construction work shall be made unless specifically authorized by this Commission.

(c) During a period of suspension of a construction project no interest charge for a longer period than 6 months from the date of its suspension shall be included in these accounts unless specifically authorized by this Commission. No such interest charges shall be included in these accounts on expenditures for construction projects which have been definitely abandoned.

(11) "Insurance" includes premiums paid or amounts credited to account 169, "Insurance reserve", for the protection against loss and damages in connection with the construction of telephone plant due to fire or other casualty, injury to or death of employees or others, damages to property of others, defalcations of employees and agents, and the nonperformance of contractual obligations of others. (Note also account 668.)

(12) "Construction services" includes the cost of telephone, electricity, power, construction quarters, office space and equipment allocated to the construction project; also similar items furnished by the company through its regular operating facilities.

22.1. Overhead construction costs.—(A) All overhead construction costs, such as engineering, supervision, general office salaries and expenses, construction engineering and supervision by others than the accounting company, law expenses, insurance, injuries and damages, relief and pensions, taxes and interest, shall be charged to particular jobs or items on the basis of the amounts of such overheads applicable thereto, to the end that each job or item shall bear its equitable proportion of such costs and that the entire cost of the item, both direct and indirect, shall be deducted from the plant accounts at the time the item of plant is retired.

(B) The records supporting the entries for overhead construction costs shall be kept so as to show the nature of the expenditures, the individual jobs and accounts charged, and the bases of the distribution. The amounts charged to each plant account for overhead costs shall be available without detailed analysis.

(C) The instructions contained herein shall not be interpreted as permitting the addition to plant accounts of arbitrary percentages or amounts to cover assumed overhead costs, but as requiring the assignment to particular jobs and accounts of actual and necessary overhead expenditures as stated in paragraph (A).

23. Improvements to leased telephone plant.—(A) Except as provided in paragraph (B) following, the cost of initial improvements (including repairs, rearrangements, additions, and betterments) to telephone plant leased from others made in the course of preparing the property for service and the cost of any subsequent additions and betterments of the leased telephone plant shall be charged to the telephone plant account appropriate for the class of property leased, unless the leasing arrangements provide that specific improvements shall be made to the leased property by the lessee and that such improvements shall revert to the lessor and constitute a part of the consideration paid for the use of the property. In the latter case, the cost of the improvements reverting to the lessor which represents payments for the use of the lessor's property shall be charged to account 129, "Prepaid rents", and cleared over the period of the lease to the appropriate accounts.

(B) When the improvements to leased telephone plant otherwise chargeable to the telephone plant accounts are of relatively minor cost or short life or the period of the lease is less than 1 year, the cost shall be charged to the account chargeable with the cost of repairs of such plant.

(C) When the cost of improvements to leased telephone plant is included in the telephone plant accounts, charges for depreciation thereof shall be made on such basis as will amortize the service value of such improvements during the period of their expected use.

24. Units of property.—The "units of property" (note also instruction 25-A-1) are listed in Appendix A. Additions to or revisions of this list will be issued, when necessary, by this Commission, to which any applications for such additions or revisions shall be presented by the company.

25. Telephone plant retired.—(aA) To the end that the telephone plant accounts (note instructions 20 and 21) shall at all times disclose the original cost (note instruction 3-8.1) of all property in service, the original cost of retired property, whether replaced or not (except as provided in paragraph (A-2) of this instruction), shall be credited to the account or accounts in this classification to which such cost was charged. Every company

shall, therefore, take such measures and establish such procedure as will insure strict compliance with these requirements. When any item of property is worn out, lost, sold, destroyed, abandoned, surrendered upon lapse of title, becomes permanently unserviceable, or is withdrawn or retired from service for any other reason, the amount in the plant accounts applicable to that item shall be credited to the appropriate plant accounts, and the retirement entry shall cite the original entry of cost of the item retired, by name and page of, or other definite identification of, book or other record in which maintained; except that, when such entry cannot be identified or is not available, that fact shall be stated in connection with the retirement entry. (Note also paragraph (D) of this instruction.)

(A) Depreciable telephone plant: For the purpose of avoiding undue refinement in accounting for the replacement of small items of property, the accounting for retirements and replacements of depreciable telephone plant shall be as follows:

(1) *Units of property.*—This group includes major items of property, a list of which is shown in Appendix A. The original cost of any such item retired shall be credited to the plant account and charged to account 171, "Depreciation reserve", whether or not replaced. (Note also paragraph (B) of account 171.) The original cost of property installed in place of the property retired shall be charged to the appropriate telephone plant account.

(2) *Minor items.*—This group includes any part or element which is not designated as a unit of property. The original cost of any minor item of property retired and not replaced shall be credited to the plant account and charged to account 171 (note also paragraph (B) of the text of that account), except that if the original cost of a minor item of property is accounted for through the retirement of units of property, no separate credit to the telephone plant account is required when such an item is retired. Except as provided in note under account 231, "Station apparatus", in Appendix A, if minor items of property are retired and replaced (apart from the unit of property of which they form a part or with which they are associated) no adjustment shall be made in account 171. The cost of the replacement shall be charged to the account appropriate for the cost of repairs of the property, except that if the replacement effects a substantial betterment (the primary aim of which is to make the property affected more useful, of greater durability, of greater capacity, or more economical in operation) the excess cost of the replacement over the estimated cost at current prices of replacing without betterment the minor items retired shall be charged to the appropriate telephone plant account.

(B) Station installations, drop and block wires: When stations are removed from customers' premises, the original cost of

the station installations carried in account 232, "Station installations", and of any drop and block wires carried in account 233, "Drop and block wires", thereby retired from service shall be credited to the plant accounts and charged to account 607, "Station removals and changes." The latter account shall be credited with the salvage value (note instruction 8–W) of such property recovered. The cost of the removal of the station apparatus, inside, drop and block wires shall be charged to account 607.

(C) Land: The original cost of land retired shall be credited to account 211, "Land." If the land is sold, the difference between such original cost and the sale price (less commissions and other expenses of making the sale) of the land shall be credited to account 401, "Credits for telephone plant sold", or debited to account 410, "Debits for telephone plant sold", as may be appropriate. If the land is retained by the company and held for sale, its cost shall be charged to account 103, "Miscellaneous physical property." The accounting for leaseholds retired shall be as provided for in the texts of account 172, "Amortization reserve", and account 613, "Amortization of intangible property."

(D) Determination of original costs: The original cost of telephone plant retired shall be the amount at which such property is included in the telephone plant accounts when such amount can be determined from the company's records. Ordinarily, such records shall be used in the retirement of land, buildings, complete central offices, furniture, and other items of plant for which individual cost records are maintained. When the actual original cost cannot be determined from the records, it shall be estimated. When it is impracticable to determine the original cost of each item due to the relatively large number or small cost of such items, the average original cost of all the items shall be used in determining the original cost of the items retired: *Provided*, however, that when classes of outside plant are subdivided between exchange and toll or by areas, the bases of such average original costs shall be confined to items comprised in the respective subdivisions. This method of average original cost may be applied in retirement of such items as telephones, bell boxes, station installations, poles, crossarms, wire, cable, cable terminals, conduit, and nonmultiple private branch exchange switchboards.

(E) The accounting for the retirement of Organization, Franchises, Patent rights, and other intangible property, shall be as provided for in the texts of account 172, "Amortization reserve", account 413, "Miscellaneous debits to surplus", account 613, "Amortization of intangible property", and account 100.4, "Telephone plant acquisition adjustment."

(F) When telephone plant is sold together with the telephone traffic associated therewith, the original cost of the property

shall be credited to the appropriate plant accounts and the estimated amounts carried with respect thereto in the depreciation and amortization reserve accounts shall be charged to such reserve accounts. The difference, if any, between (a) the net amount of such debit and credit items and (b) the consideration received (less commissions and other expenses of making the sale) for the property shall be included, if a debit, in account 410, "Debits for telephone plant sold", and if a credit, in account 401, "Credits for telephone plant sold." The accounting for depreciable telephone plant sold without the traffic associated therewith shall be in accordance with the accounting provided in paragraph (B) of account 171, "Depreciation reserve."

26. Telephone plant continuing property record required.—(A) Not later than January 1, 1936, each company shall begin the preparation of a continuing or perpetual detailed record of telephone plant. This record shall be completed not later than December 31, 1936.

(B) The record shall be arranged in conformity with the telephone plant accounts prescribed in this classification. It shall be compiled on the basis of original cost (note instruction 3-8.1) and shall contain such detailed description and classification of the property units as will permit [redacted] ready verification.

Income Accounts

30. Purpose of income accounts.—The income accounts (300 to 344, inclusive) are designed to show as nearly as practicable for each calendar year the total operating revenues and operating expenses of the company; the returns accrued upon securities owned and from property not used in the company's operations; the amounts accrued for taxes, use of moneys, and use of operating properties of others; and reservations and appropriations of income. (Note also instructions 4, 5, and 6.)

31. Income from sinking and other funds.—When interest and other income arising from funds carried in account 104, "Sinking funds", account 136, "Provident funds", or account 137, "Insurance and other funds", (note also account 314) are required by the mortgage or other provisions to be held in the funds, they shall be charged to those accounts. If such funds are represented by a reserve established through reservations of income or surplus, amounts so set aside shall be charged to account 342, "Contractual reservations of income", account 343, "Miscellaneous reservations of income", account 414, "Contractual reservations of surplus", or account 415, "Miscellaneous reservations of surplus", and credited to account 169, "Insurance reserve", account 170, "Provident reserve", account 173, "Employment stabilization reserve", or account 180, "Surplus reserved", as may be appropriate.

Surplus Accounts

40. **Purpose of surplus accounts.**—The surplus accounts (400 to 416, inclusive) are designed to show the changes in the company's surplus or deficit during each calendar year resulting from (a) the operations and other transactions during that period reflected in the income accounts, (b) appropriations or other reservations of surplus for specific purposes, (c) accounting adjustments not properly attributable to the period (note also instruction 5), and (d) miscellaneous losses and gains not provided for elsewhere. The balance of the surplus accounts (400 to 416, inclusive) shall be closed into account 181, "Unappropriated surplus", at the end of each calendar year.

Operating Revenue Accounts

50. **Purpose of operating revenue accounts.**—(A) The operating revenue accounts (500 to 539, inclusive) are designed to show the amounts of money which the company becomes lawfully entitled to receive, less uncollectible revenues, from the furnishing of telephone service (including operations incidental thereto). Credits to the various revenue accounts shall be based upon the actual amounts chargeable for services rendered by the company. It is not required that undetermined amounts of revenue at pay stations lost through fire, theft, or collection of slugs or coins having no legal tender value shall be included in the operating revenue accounts. (Note also instructions 4, 5, and 6, and account 650.)

(B) In addition to monthly service charges, the operating revenue accounts appropriate for the class of service involved shall be credited with:

(1) Amounts charged for connection, restoration and termination of service, and for inside moves, outside moves, instrument changes and similar service requirements.

(2) Amounts of initial nonrecurring charges for special or auxiliary plant or equipment furnished in rendering service to a customer, except that charges for the cost of providing plant or equipment the ownership of which rests with or will revert to the customer shall be credited to the accounts charged with the cost of such plant or equipment.

(3) Amounts of service charges for supplemental or auxiliary equipment furnished in rendering service to a customer—for example, extension stations, auxiliary receivers, auxiliary signals, code calling and conference equipment, etc.

(C) The classification of operating revenues provides separate accounts for local revenue and for toll revenue. In case it is necessary to apportion the revenue between these accounts, the company shall be prepared when so required by this Commission to furnish the basis used in making such apportionment.

51. **Deductions from revenues.**—Discounts allowed customers for prompt payment, corrections of overcharges, authorized refunds of overcollections theretofore credited, authorized refunds and adjustments on account of failures in service, and other corrections shall be charged to the revenue account previously credited with the amounts involved.

52. **Commissions.**—(A) Commissions paid to employees or others in place of salaries or other compensation for services rendered, such as public telephone commissions, shall be charged to the appropriate expense accounts and not to the revenue accounts.

(B) Originating and other commissions representing divisions of operating revenues between telephone companies shall be accounted for through the appropriate operating revenue accounts.

Operating Expense Accounts

60. **Purpose of operating expense accounts.**—The operating expense accounts (602.1 to 677, inclusive) are designed to show the expenses of furnishing telephone service (note instruction 3-AA), including expense of maintaining the plant used in such service. (Note also instructions 4, 5, and 6.)

61. **Cost of repairs.**—(A) The cost of repairs chargeable to the various operating expense and clearing accounts includes: Inspecting, testing, and reporting on the condition of telephone plant to determine the need for repairs, replacements, rearrangements, and changes; testing for, locating and clearing trouble; routine work (note also paragraph B) to prevent trouble, such as pulling up slack, tightening guys and raking guy stubs, trimming trees, straightening poles and crossarms, and cleaning and adjusting equipment; replacing minor items of telephone plant (note also instruction 25); rearranging and changing the location of property not retired; repairing material for reuse; restoring the condition of property damaged by storms, floods, fire, or other casualties (note also paragraph B); training employees for maintenance work; inspecting and testing after repairs have been made; and an equitable proportion of the cost of local plant administration, general plant supervision and engineering.

(B) The cost of repairs does not include the cost of replacing items of property designated as "units of property" except as provided in account 605, "Repairs of station equipment", for labor and incidental costs in the replacement of station apparatus. (Note also instruction 25.)

62. **Joint operating expenses.**—(A) In accounting for operating expenses incurred under arrangements for joint participation or apportionment between telephone companies, the creditor company shall charge initially the entire expense to the appropriate primary accounts. The proportion of such expenses borne by the

debtor shall be credited by the creditor and charged by the debtor to the accounts initially charged, except that by agreement between the participating companies the proportion of traffic expenses borne by the debtor may be credited by the creditor to account 635, "Joint traffic expenses—Cr.", and charged by the debtor to account 634, "Joint traffic expenses—Dr."

(B) Any allowances for return on the property used under the arrangement shall be credited by the creditor to the appropriate rent revenue account and charged by the debtor to the appropriate rent expense account.

(C) The creditor company shall inform the debtor company of the distribution of charges made by it.

63. **Distribution of pay and expenses of employees.**—(A) Charges to the telephone plant, operating expense, and other accounts for services and expenses of employees engaged in activities chargeable to various accounts shall be based upon the actual time engaged in the respective classes of work except that the pay and expenses of an employee who performs the same class of work from day to day may be distributed upon the basis of a study of the time actually engaged during a representative period.

(B) The pay and expenses of employees of one department who perform for another department incidental services involving only small expense shall be included in the expenses of the department in which the employees are regularly employed.

64. **Extensive replacements.**—When it becomes necessary to replace the majority of either station apparatus, inside, drop, or block wires, in any given central office district, together with any number of such items in contiguous districts, the cost of the replacements chargeable to account 605, "Repairs of station equipment", if so authorized by this Commission upon application to it, shall be charged to account 138, "Extraordinary maintenance and retirements", and cleared to account 605 over the period specified in the authority.

Clearing Accounts

70. **Purpose of clearing accounts.**—The clearing accounts (702 to 707, inclusive) are provided as a medium for the distribution of certain items which affect more than one primary account and which cannot be appropriately allocated as they are incurred. (Note also instruction 2-C.)

Depreciation Accounting

80. **Computation of depreciation rates.**—(A) Depreciation charges shall be computed by applying the composite annual percentage rates considered applicable to the original cost (note in-

struction 3–S.1) of each class of depreciable telephone plant owned or used by the company. (Note also instruction 81–B.) These percentage rates shall be based upon the estimated service values and service lives (note instruction 3–Y–X) developed by a study of the company's history and experience and such engineering and other information as may be available with respect to prospective future conditions. These percentage rates shall be computed in conformity with the group plan (note instruction 3–L) of accounting for depreciation and shall be such that the loss in service value of the property, except for losses excluded under the definition of depreciation (note instruction 3–J), may be distributed under the straight-line method (note instruction 3–Z) during the service life of the property. Such percentage rates shall not include any allowance for loss in service value of property expected to be installed in the future. The percentage rates shall, for each primary account comprised of more than one class of property, produce a charge to operating expenses for that account equal to the sum of the amounts that would otherwise be chargeable for each of the various classes of property included in the account.

(B) In the event any composite percentage rate becomes no longer applicable, revised composite percentage rates shall be computed in accordance with paragraph (A) of this instruction.

(C) The company shall keep such records of property and property retirements as will reflect the service life of property which has been retired, or will permit the determination of service-life indications by mortality, turnover, or other appropriate methods, and also such records as will reflect the percentage of salvage value, or net salvage value, as appropriate, for property retired from each class of depreciable telephone plant.

81. Depreciation charges.—(A) Charges for currently accruing depreciation shall be made monthly to account 608, "Depreciation", and to clearing accounts, as appropriate, and corresponding credits shall be made to account 171, "Depreciation reserve." In computing the current monthly charges, one-twelfth of the composite annual percentage rate applicable to the primary accounts covering depreciable telephone plant shall be applied to the average of the balances, as of the first and last of the current month, in each such primary account.

(B) When the company is responsible under the terms of a lease for depreciation of property, used but not owned, for which the rent is chargeable to account 303, "Rent for lease of operating property", depreciation charges shall be made on the same basis as for owned depreciable property.

(C) A separate composite annual percentage rate for each account covering depreciable telephone plant shall be used in com-

puting depreciation charges. Such composite rates shall be computed in accordance with instruction 80.

82. **Classes of depreciable telephone plant.**—The classes of depreciable telephone plant and the accounts covering such plant are as follows:

Right of way (account 207).
Buildings (account 212).
Central office equipment (account 221).
Station apparatus (account 231).
Private branch exchanges (account 234).
Booths and special fittings (account 235).
Pole lines (account 241).
Aerial cable (account 242.1).
Underground cable (account 242.2).
Buried cable (account 242.3).
Submarine cable (account 242.4).
Aerial wire (account 243).
Underground conduit (account 244).
Furniture and office equipment (account 261).
Vehicles and other work equipment (account 264).

NOTE.—When depreciable plant carried in account 276, "Telephone plant acquired", is distributed to the appropriate plant accounts, adjusting entries shall be made covering the depreciation charges applicable to such plant for the period during which it was carried in account 276.

83. **Plant retired for causes not factors in depreciation.**—The service value of depreciable telephone plant retired (note also instruction 25) shall be charged in its entirety to account 171, "Depreciation reserve." If the cause of retirement is not a recognized factor in depreciation (note instruction 3–J) and the loss is not covered by insurance, the company may, upon proof that the charge to the depreciation reserve will result in undue depletion thereof, and with the approval of this Commission, credit account 171, "Depreciation reserve", and charge account 138, "Extraordinary maintenance and retirements", with the unprovided-for loss in service value and distribute it from that account to account 609, "Extraordinary retirements", over such period as this Commission may approve.

BALANCE-SHEET STATEMENT

Asset Side

I. Investments:

100.1. Telephone plant in service.
100.2. Telephone plant under construction.
100.3. Property held for future telephone use.
100.4. Telephone plant acquisition adjustment.
101.1. Investments in affiliated companies.
101.2. Advances to affiliated companies.
102. Other investments.
103. Miscellaneous physical property.
104. Sinking funds.
105. Company securities owned.

II. Current Assets:

113. Cash.
114. Special cash deposits.
115. Working funds.
116. Temporary cash investments.
117.1. Notes receivable from affiliated companies.
117.2. Other notes receivable.
118. Due from customers and agents.
120.1. Accounts receivable from affiliated companies.
120.2. Other accounts receivable.
121. Interest and dividends receivable.
122. Material and supplies.
123. Other current assets.

III. Other Assets:

126. Subscriptions to capital stock.
127. Subscriptions to funded debt.

IV. Prepaid Accounts and Deferred Charges:

129. Prepaid rents.
130. Prepaid taxes.
131. Prepaid insurance.
132. Prepaid directory expenses.
133. Other prepayments.
134.1. Discount on capital stock.
134.2. Capital stock expense.
135. Discount on long-term debt.
136. Provident funds.
137. Insurance and other funds.
138. Extraordinary maintenance and retirements.
139. Other deferred charges.

LIABILITY SIDE

V. STOCK:

150. Capital stock.
151. Stock liability for conversion.
152. Premium on capital stock.
153.1. Capital stock subscribed.
153.2. Installments paid on capital stock.

VI. LONG-TERM DEBT:

154.1. Funded debt.
154.2. Funded debt subscribed.
155. Receivers' certificates.
156. Advances from affiliated companies.
157. Other long-term debt.

VII. CURRENT LIABILITIES:

158.1. Notes payable to affiliated companies.
158.2. Other notes payable.
159.1. Accounts payable to affiliated companies.
159.2. Other accounts payable.
160. Customers' deposits.
162. Matured interest and dividends.
163. Matured long-term debt.
164. Advance billing and payments.
165. Other current liabilities.

VIII. ACCRUED LIABILITIES NOT DUE:

166. Taxes accrued.
167. Unmatured interest, dividends, and rents accrued.

IX. DEFERRED CREDITS AND RESERVES:

168. Premium on long-term debt.
169. Insurance reserve.
170. Provident reserve.
171. Depreciation reserve.
172. Amortization reserve.
173. Employment stabilization reserve.
174. Other deferred credits.

X. CONTRIBUTIONS OF TELEPHONE PLANT:

175. Contributions of telephone plant.

XI. SURPLUS:

180. Surplus reserved.
181. Unappropriated surplus.

BALANCE-SHEET ACCOUNTS

(Note particularly instructions 10 to 17, inclusive)

I. INVESTMENTS

100.1. Telephone plant in service.—This account shall include the original cost (note instruction 3–S.1) of the company's prop-

erty used in telephone service at the date of the balance-sheet as classified under accounts 201 to 277, inclusive. (Note also instructions 3–AA, 20, and 21.)

100.2. **Telephone plant under construction.**—(A) This account shall include the original cost (note instruction 3–S.1) of construction of telephone plant not completed ready for service at the date of the balance-sheet. It shall include interest during construction, taxes during construction, and all other elements of cost of such construction work. (Note also instructions 20, 21, and 22.)

(B) When any telephone plant the cost of which has been included in this account is completed ready for service, the cost thereof shall be credited to this account and charged to the appropriate telephone plant or other accounts.

NOTE.—It is not required that this account shall include the cost of construction work which will be completed ready for service within a short period, such as the installation of station apparatus, replacements of poles, and other work completed within a period of one or two months.

100.3. **Property held for future telephone use.**—(A) This account shall include the original cost (note instruction 3–S.1) of property owned and held for imminent use in telephone service under a definite plan for such use.

(B) The property included in this account shall be classified according to the primary accounts for telephone plant in service. Separate subaccounts shall be provided for this purpose which accounts shall carry the same numbers as the plant accounts except that each account shall be prefixed by (1). (Note also instructions 20 and 21.)

100.4. **Telephone plant acquisition adjustment.**—(A) This account shall include the difference between (a) the amount of money actually paid (or the current money value of any consideration other than money exchanged) for telephone plant acquired, plus preliminary expenses incurred in connection with the acquisition; and (b) the original cost (note instruction 3–S.1) of such plant, governmental franchises and similar rights acquired, less the amounts of reserve requirements for depreciation and amortization of the property acquired, and amounts of contributions to the predecessor company or companies for construction and acquisition of such property. If the actual original cost is not known, the entries in this account shall be based upon an estimate of such cost. (Note also instruction 21.)

(B) This account shall be subdivided according to the character of the amounts contained therein. In addition to a copy of the journal entry recorded to open the account, the company shall file with this Commission statements showing the basis of the computation of amounts included therein. The detailed rec-

ords supporting these statements shall be retained permanently by the company.

(C) The amounts recorded in this account with respect to each property acquisition shall be disposed of, written off, or provision shall be made for the amortization thereof in such manner as this Commission may direct. (Note also instruction 21.)

101.1. **Investments in affiliated companies.**—(A) This account shall include the book cost (note instruction 12) of the company's investment in securities issued or assumed by affiliated companies (note instruction 3–D) other than securities held in special funds (see also note B to this account) or as temporary cash investments.

(B) This account shall be maintained so as to show separately the book cost of:

(1) Common stocks.
(2) Preferred stocks.
(3) Long-term debt.

(C) The company's records shall be kept in such manner that in the annual reports to this Commission the securities pledged as collateral security for any of the company's long-term debt or short-term loans or to secure performance of contracts may be shown separately from securities unpledged.

NOTE A.—The value of securities borrowed by the company shall not be included in this account.

NOTE B.—The book cost of securities held in special funds shall be included in accounts 104, 136, or 137, as may be appropriate.

NOTE C.—Working funds advanced to affiliated companies other than investment advances (note instruction 3–M) shall be included in account 115.

101.2. **Advances to affiliated companies.**—This account shall include the amount of the investment advances (note instruction 3–M) to affiliated companies.

NOTE.—Amounts receivable from affiliated companies which are subject to current settlement shall be included in accounts 117.1 or 120.1, as appropriate.

102. **Other investments.**—(A) This account shall include the book cost (note instruction 12) of the company's investment in securities issued or assumed by nonaffiliated companies (note instruction 3–S) and individuals, other than securities held in special funds (see also note C to this account) or as temporary cash investments; also its investment advances (note instruction 3–M) to such parties and special deposits of cash for more than 1 year from date of deposit.

(B) This account shall be maintained so as to show separately the book cost of:

(1) Stocks.
(2) Long-term debt.

(3) Investment advances.

(4) Special deposits of cash for more than 1 year from date of deposit.

(C) The company's records shall be kept in such manner that in the annual reports to this Commission the securities pledged as collateral security for any of the company's long-term debt or short-term loans or to secure the performance of contracts may be shown separately from the securities unpledged.

NOTE A.—Amounts receivable from nonaffiliated companies and individuals which are subject to current settlement shall be included in accounts 117.2 or 120.2, as appropriate.

NOTE B.—The value of securities borrowed by the company shall not be included in this account.

NOTE C.—The book cost of securities held in special funds shall be included in accounts 104, 136, or 137, as may be appropriate.

NOTE D.—Working funds advanced to nonaffiliated companies and individuals other than investment advances (note instruction 3–M) shall be included in account 115.

103. **Miscellaneous physical property.**—This account shall include the company's investment in physical property other than property the investment in which is includible in accounts 100.1, "Telephone plant in service", 100.2, "Telephone plant under construction", and 100.3, "Property held for future telephone use." It shall include the company's investment in telephone property retired (note instruction 3–T) and held for sale; also property such as lighting, water, power, and manufacturing plants, not held incident to the company's telephone operations, and assessments against miscellaneous physical property for the construction of public improvements.

104. **Sinking funds.**—(A) This account shall include the amount of cash, the book cost of securities issued by other companies, and the book or face amount (note instruction 3–D.1–K.1) of nominally issued and nominally outstanding (note instruction 3–Q–R) securities issued or assumed by the company, and other assets which are held by trustees or by the company's treasurer in a distinct fund, for the purpose of redeeming outstanding obligations. (Note also instructions 12, 13, and 31.)

(B) A separate account shall be kept for each sinking fund under a title which shall designate the obligation in support of which the fund was created.

105. **Company securities owned.**—(A) This account shall include the book or face amount (note instruction 3–D.1–K.1) of nominally issued and nominally outstanding (note instruction 3–Q–R) securities issued or assumed by the company, other than such securities held in sinking or other special funds. (Note also instruction 13.)

(B) This account shall be maintained so as to show:

(1) For stock:

(a) Par stock:

(1) Number of shares and total book amount of shares unpledged.

(2) Number of shares and total book amount of shares pledged.

(b) Nonpar stock: (Note instruction 16.1.)

(1) Number of shares and book amount assigned to shares unpledged.

(2) Number of shares and book amount assigned to shares pledged.

(2) For long-term debt:

(a) Total face amount unpledged.

(b) Total face amount pledged.

II. Current Assets

113. Cash.—This account shall include the amount of current funds available for use on demand in the hands of financial officers and agents, or deposited in banks or with trust companies, also funds in transit for which agents have received credit. (Note also instruction 11.)

Note.—Working funds shall be included in account 115.

114. Special cash deposits.—This account shall include the amount of cash on special deposit, other than in sinking and other special funds provided for elsewhere, to pay dividends, interest, and other debts, when such payments are due 1 year or less from the date of deposit; the amount of cash deposited to insure the performance of contracts to be performed within 1 year from date of the deposit; and other cash deposits of a special nature not provided for elsewhere. This account shall include the amount of cash deposited with trustees to be held until mortgaged property sold, destroyed, or otherwise disposed of is replaced, and also cash realized from the sale of the company's securities and deposited with trustees to be held until invested in physical property of the company or for disbursement when the purposes for which the securities were sold are accomplished. (Note also instruction 11.)

Note A.—Cash on deposit in special accounts where the funds are available for the current requirements of the company shall be included in account 113.

Note B.—This account shall not include any amounts representing securities owned.

Note C.—Cash on special deposit to be held for more than 1 year from the date of deposit shall be included in account 102.

115. **Working funds.**—This account shall include amounts advanced to officers, employees, and others as working funds from which certain expenditures are to be made and accounted for. (Note also instruction 11.)

116. **Temporary cash investments.**—This account shall include the book cost (note also instructions 11 and 12) of securities acquired for the purpose of temporarily investing cash, such as time drafts receivable and time loans, bankers' acceptances, United States Treasury certificates, marketable securities, and other similar investments of a temporary character. Securities of affiliated companies included in this account shall be recorded in a subaccount hereunder.

117.1. **Notes receivable from affiliated companies.**—This account shall include the book cost (note instruction 12) of demand or time notes, bills and drafts receivable, or other similar evidences (except interest coupons) of money receivable from affiliated companies on demand or within a time not exceeding 1 year from date of issue. (Note also instruction 11.)

NOTE.—Obligations of affiliated companies any part of which matures more than 1 year from date of issue and notes evidencing investment advances (note instruction 3–M) shall be included in accounts 101.1, 101.2, 104, 116, 136, or 137, as appropriate.

117.2. **Other notes receivable.**—This account shall include the book cost (note instruction 12) not includible elsewhere, of all collectible obligations from nonaffiliated companies and individuals in the form of notes receivable and other similar evidences (except interest coupons) of money receivable on demand or within a time not exceeding 1 year from date of issue. (Note also instruction 11.)

NOTE.—Obligations any part of which matures more than 1 year from date of issue, notes evidencing investment advances (note instruction 3–M) and notes issued by affiliated companies shall be included in accounts 101.1, 101.2, 102, 104, 116, 117.1, 136, or 137, as appropriate.

118. **Due from customers and agents.**—This account shall be subdivided as follows:

(A) Due from customers and agents.

(1) This subaccount shall include amounts due from customers for services rendered or billed and from agents and collectors authorized to make collections from customers. (Note also instruction 11.) This subaccount shall be kept in such manner as will enable the company to make the following analysis:

(a) Amounts due from customers who are still receiving telephone service.

(b) Amounts due from customers whose telephone service has been discontinued and whose accounts are in process of collection.

(2) Collections in excess of amounts charged to this subaccount may be credited to and carried in this account until applied against charges for services rendered or until refunded.

(3) The amount of notes held as security for customers' accounts may be carried in this account pending collection.

(B) Reserve for uncollectible accounts.—Cr.

(1) This subaccount shall be credited with such amounts as may be charged to account 530, "Uncollectible operating revenues—Dr.", to provide for uncollectible accounts included in subaccount 118–A. (Note also instruction 51.) There shall also be credited to this subaccount amounts collected which previously have been written off through charges to this subaccount and credits to subaccount 118–A.

(2) If this reserve for uncollectible accounts is maintained, there shall be charged to it any amounts covered thereby which have been found to be impracticable of collection. If such reserve is not maintained, amounts included in subaccount 118–A which have been found to be uncollectible shall be charged to account 530, "Uncollectible operating revenues—Dr."

120.1. **Accounts receivable from affiliated companies.**—(A) This account shall include amounts due from affiliated companies (note instruction 3–D) on all transactions that are subject to current settlement, except for sales of telephone service at regular rates. There shall be included herein accounts receivable arising from divisions of toll revenues. (Note also instruction 11.)

(B) In the balance-sheet statement there may be included in this account the net amount receivable from companies against each of which there is a net debit balance between this account and account 159.1, "Accounts payable to affiliated companies."

NOTE.—If any items included in this account are not actually paid currently they shall be transferred to account 101.2.

120.2. **Other accounts receivable.**—(A) This account shall include all amounts currently due, other than those from affiliated companies, and not provided for in other accounts, such as those for traffic settlements, material and supplies, repairs to telephone plant, matured rents, and interest receivable under monthly settlements on short-term loans, advances, and open accounts. (Note also instruction 11.)

(B) In the balance-sheet statement there may be included in this account the net amount receivable from companies against each of which there is a net debit balance between this account and account 159.2, "Other accounts payable."

121. **Interest and dividends receivable.**—This account shall include the amount of interest accrued to the date of the balance-sheet on bonds, notes, and other commercial paper owned, on

loans made, and the amount of dividends receivable on stocks owned. (Note also instruction 11.)

NOTE A.—These accounts shall not include dividends or other returns on securities issued or assumed by the company and held by or for it, whether pledged as collateral, or held in its treasury, in special deposits, or in sinking and other funds.

NOTE B.—Interest receivable under monthly settlements on short-term loans, advances, and open accounts, shall be included in accounts 120.1 or 120.2, as appropriate.

122. **Material and supplies.**—(A) This account shall include the cost of unapplied material and supplies held in stock, including plant supplies, tools, fuel, stationery, directory paper stock, and other supplies; and material and articles of the company in process of manufacture for supply stock.

(B) Transportation charges, so far as practicable, shall be included as a part of the cost of the particular material to which they relate. When not so includible, they shall be charged to account 704, "Supply expense."

(C) So far as practicable, cash and other discounts on material shall be deducted in determining the cost of the particular material to which they relate or credited to the account to which the material is charged. When not so deductible, they shall be credited to account 704, "Supply expense."

(D) Material recovered in connection with construction, maintenance, or retirement of property shall be charged to this account as follows (note instruction 3-W):

(1) Reusable material shall be included in this account at original cost (note instruction 3-S.1), estimated if not known. (Note also instruction 25-D.) The cost of repairing such material shall be charged to the appropriate account in operating expenses.

(2) Scrap and nonusable material included in this account shall be carried at the estimated amount which will be received therefor. The difference between the amounts realized for scrap and nonusable material sold and the amounts at which it is carried in this account, so far as practicable, shall be adjusted in the accounts credited when the material was taken up in this account.

NOTE A.—This account shall not include amounts representing the cost of material or articles, title to which is not vested in the company.

NOTE B.—Interest paid on material bills, the payments of which are delayed, shall be charged to account 336.

NOTE C.—Inventories of material and supplies shall be taken during each calendar year and the necessary adjustment to bring this account into harmony with the actual inventory shall be made. In effecting this adjustment, differences which may practically be assigned to important classes of material shall be equitably adjusted among the accounts to which the classes of material are ordinarily chargeable. Other differences shall be equitably apportioned among the primary accounts to which material has been charged since the last inventory or included in account 704. The

company is permitted to equalize over the period between inventories, through debits or credits to account 704 and concurrent credits or debits to account 122, the estimated amount, based on the company's past experience, of the overage or shortage which will occur at the subsequent inventory. Determined differences between the amount of the provision thus made and the actual inventory overage or shortage shall be cleared as provided for in the second and third sentences of this note.

NOTE D.—If, for convenience in accounting and economy in handling material and supplies for nontelephone operations, their cost is included in this account, the company's records shall be maintained so that the cost of such material and supplies so carried can be determined.

123. **Other current assets.**—This account shall include the amount of all current assets which are not includible in accounts 113 to 122, inclusive, such as unmatured rents receivable. (Note also instruction 11.)

III. OTHER ASSETS

126. **Subscriptions to capital stock.**—(A) This account shall include the balance owing from subscribers upon legally enforceable subscriptions to capital stock.

(B) The purchase price shall be debited to this account at the time the subscription is received. Concurrently there shall be credited to account 153.1, "Capital stock subscribed", the book amount (note instruction 3-D.1) of the stock subscribed. The difference between these amounts shall be debited or credited, as appropriate, to account 134.1, "Discount on capital stock", or account 152, "Premium on capital stock." (Note also instruction 3-K-U.)

(C) Payments received from subscribers shall be credited to this account.

NOTE.—The records supporting the entries to this account shall be kept so that the company can furnish the name and address of each subscriber, the amount and kind of capital stock subscribed, the date of subscription, the date that each payment is due and the date that each is paid, the nature of each payment (whether cash or other consideration), and any other information that is necessary to make the history of the subscription complete.

127. **Subscriptions to funded debt.**—(A) This account shall include the balance owing from subscribers upon legally enforceable subscriptions to funded debt.

(B) The purchase price shall be debited to this account at the time the subscription is received. Concurrently there shall be credited to account 154.2, "Funded debt subscribed", the face amount (note instruction 3-K.1) of the funded debt subscribed. The difference between these amounts shall be debited or credited, as appropriate, to account 135, "Discount on long-term debt", or account 168, "Premium on long-term debt." (Note also instruction 3-K-U.)

(C) Payments received from subscribers shall be credited to this account.

NOTE.—The records supporting the entries to this account shall be kept so that the company can furnish the name and address of each subscriber, the amount and kind of funded debt subscribed, the date of subscription, the date that each payment is due and the date that each is paid, the nature of each payment (whether cash or other consideration), and any other information that is necessary to make the history of the subscription complete.

IV. PREPAID ACCOUNTS AND DEFERRED CHARGES

129. **Prepaid rents.**—This account shall include the amounts of rents paid in advance, except minor amounts which may be charged direct to the final accounts. As the term expires for which the rents are paid, this account shall be credited at monthly intervals and the appropriate account charged. (Note also instructions 22–B, 23–A, and accounts 303, 315, 671, and the clearing accounts.)

130. **Prepaid taxes.**—This account shall include the amounts of taxes paid in advance, except minor amounts which may be charged direct to the final accounts. As the term expires for which the taxes are paid, this account shall be credited at monthly intervals and the appropriate account charged. (Note also instruction 22–B–8 and accounts 305 and 322.)

131. **Prepaid insurance.**—This account shall include the amount of insurance premiums paid in advance, except premiums chargeable to the telephone plant accounts and minor amounts which may be charged direct to the final accounts. As the term expires for which the premiums are paid, this account shall be credited at monthly intervals and the appropriate account charged.

132. **Prepaid directory expenses.**—This account shall include the cost of preparing, printing, binding, and delivering directories and the cost of soliciting advertisements for directories, except minor amounts which may be charged direct to account 649, "Directory expenses." Amounts carried in this account shall be cleared to account 649 by monthly charges of such amounts as represent the portion of the expense that is applicable to the respective months. (Note also account 649.)

133. **Other prepayments.**—This account shall include prepayments other than those includible in accounts 129 to 132, inclusive, except minor amounts which may be charged direct to the final accounts. As the term expires for which the payments apply, this account shall be credited at monthly intervals and the appropriate account charged.

134.1. **Discount on capital stock.**—This account shall include the total of debit balances in the discount and premium accounts,

for all classes of capital stock having debit balances in these accounts. (Note instruction 14.)

134.2. **Capital stock expense.**—(A) This account shall include all commissions and expenses incurred in connection with the issuance, sale, or resale of capital stock, including additional capital stock of a certain class or series as well as first issues. (Note instructions 3–Y.1 and 13–B.)

(B) When any issue of capital stock, or a portion thereof, is reacquired, there shall be credited to this account and charged to account 413, "Miscellaneous debits to surplus", the amount herein with respect to such stock.

(C) The company may amortize or write off the balance carried in this account by credits hereto and concurrent charges to account 413, "Miscellaneous debits to surplus."

(D) Separate subaccounts shall be provided hereunder for each class and series of capital stock.

135. **Discount on long-term debt.**—This account shall include the total of debit balances in the discount, premium, and debt expense accounts, for all classes of long-term debt having debit balances in these accounts. (Note instruction 15.)

136. **Provident funds.**—This account shall include the amount of cash, the book cost of securities of other companies, and the book or face amount (note instruction 3–D.1–K.1) of nominally issued and nominally outstanding (note instruction 3–Q–R) securities issued or assumed by the company, and other assets held by trustees or managers of employees' pension funds, savings funds, relief, hospital, and other association funds (whether contributed by the company, by employees, or by others), when such trustees or managers are acting for the company in the administration of such funds. (Note also instructions 12, 13, and 31.)

NOTE.—This account shall not include funds held by trustees when such funds are irrevocably devoted to pension purposes.

137. **Insurance and other funds.**—This account shall include the amount of cash, the book cost of securities of other companies, and the book or face amount (note instruction 3–D.1–K.1) of nominally issued and nominally outstanding (note instruction 3–Q–R) securities issued or assumed by the company, and other assets held by trustees or managers (including workmen's compensation commissions) of insurance and other funds which have been specifically set aside or invested for specific purposes not provided for elsewhere. A separate account shall be kept for each fund under titles which will designate the obligation in support of which the fund is created. (Note also instructions 12, 13, and 31.)

138. **Extraordinary maintenance and retirements.**—(A) This account shall include the unprovided-for loss in service value of

telephone plant retired in accordance with provisions of instruction 83. (Note also account 609.)

(B) This account shall include also the cost of extensive replacements of station apparatus, inside, drop and block wires, in accordance with the provisions of instruction 64. (Note also account 605.)

(C) Charges provided in paragraphs (A) and (B) shall be included in this account only after permission of this Commission has been obtained. The company's application to this Commission for such permission shall give full particulars concerning the property retired or of the extensive replacements of apparatus or wires, the amount chargeable to operating expenses, and the period over which in its judgment the amount of such charges should be distributed.

139. **Other deferred charges.**—This account shall include all deferred charges, not provided for elsewhere, such as unaudited amounts and other debit balances in suspense that cannot be cleared and disposed of until additional information is received; debit balances in clearing accounts; the amount, pending determination of loss, of funds on deposit with banks which have failed; assets of current character but of doubtful value (note also instruction 11); revenue, expense, and income items held in suspense (note also instruction 6); amounts paid for options pending final disposition; the cost of preliminary surveys, plans, investigations, etc., made for determining the feasibility of projects under contemplation. This account shall include also the cost of valuations, inventories, and appraisals taken in connection with the contemplated acquisition or sale of property. If the property is subsequently acquired, the preliminary costs shall be accounted for as a part of the cost of acquisition, or if it is sold, such costs shall be deducted from the sale price in accounting for the property sold. If contemplated projects are carried out, the preliminary costs shall be included in the cost of the projects; if the contemplated projects are abandoned, such costs (including options paid, if any) shall be charged to account 413, "Miscellaneous debits to surplus."

V. Stock

150. **Capital stock.**—(A) This account shall include the book amount (note instruction 3–D.1) of certificates which represent permanent interests in the company or interests which if terminable are so only at the option of the company. (Note also instruction 16.1.)

(B) This account shall be kept so as to show the book amount of: (1) Nominally issued capital stock, (2) actually outstanding capital stock, and (3) nominally outstanding capital stock. (Note instructions 3–C–Q–R and 13–B.)

(C) The amounts included herein shall be further divided so as to show the book amount of stocks with par value and stocks without par value, classified according to preferences in distribution of dividends or assets, difference in voting rights, and difference in conditions under which they may be retired.

(D) This account shall be charged with the book amount of any stock retired at the time of retirement.

NOTE A.—When a general levy or assessment is made against holders of par stock requiring the payment of any sum in addition to the consideration agreed upon at the time of the sale, the amount collected upon such levy or assessment shall be credited to the discount or premium account for the class of stock on which the assessment is made. If such a levy or assessment is made against the holders of nonpar stock, the amount collected shall be added to the book amount carried in this account for such stock.

NOTE B.—No debits shall be made to this account for nonpar stock except for the retirement of the stock or for amounts distributed to stockholders in liquidation.

NOTE C.—No entries shall be made in this account for stock certificates before the certificates have been lawfully authorized and authenticated.

151. **Stock liability for conversion.**—This account shall include the company's liability under agreements to exchange its capital stock for the outstanding securities of other companies which have not been surrendered for exchange.

NOTE.—When prior to their actual conversion the securities outstanding have been given all rights and privileges of capital stock of the company's own issue, such securities shall be included in account 150.

152. **Premium on capital stock.**—This account shall include the total of credit balances in the discount and premium accounts, for all classes of capital stock having credit balances in these accounts. (Note instruction 14.)

153.1. **Capital stock subscribed.**—(A) This account shall include the book amount (note instruction 3–D.1) of capital stock for which legally enforceable subscriptions have been received but for which, at the date of the balance-sheet, stock certificates have not been issued. A separate subaccount shall be maintained for each class of capital stock.

(B) This account shall be debited and account 150, "Capital stock", credited when a subscriber has paid his subscription in full and stock certificates are issued representing the shares subscribed.

(C) Accrued dividends, if any, on the stock certificates issued to subscribers shall be accounted for through the appropriate dividend, discount, or premium account. (Note instruction 3–K–U, also account 126.)

153.2. **Installments paid on capital stock.**—(A) This account shall include the amount of installments paid on capital stock on

a partial or installment payment plan by subscribers against whom there is no legally enforceable subscription contract, and who are entitled to be reimbursed for the principal amount of their payments, with or without interest, in the event they fail to complete payments for the stock and receive certificates therefor.

(B) As the total amount of each subscription is received and stock certificates are issued this account shall be cleared; the book amount (note instruction 3-D.1) of the certificates shall be included in account 150, "Capital stock", and any discount or premium (note instruction 3-K-U) involved shall be included in the appropriate discount or premium account.

NOTE.—The records supporting the entries to this account shall be kept so that the company can furnish the name and address of each subscriber, the amount and kind of capital stock subscribed, the date of subscription, the date that each payment is due and the date that each is paid, the nature of each payment (whether cash or other consideration), and any other information that is necessary to make the history of the subscription complete.

VI. LONG-TERM DEBT

154.1. **Funded debt.**—(A) This account shall include the total face amount (note instruction 3-K.1) of unmatured debt, maturing more than 1 year from date of issue, issued by the company and not retired, and the total face amount of similar unmatured debt of other companies, the payment of which has been assumed by the company, including funded debt the maturity of which has been extended by specific agreement. (Note instructions 13 and 15, also account 154.2.)

(B) This account shall be kept so as to show the face amount of: (1) Nominally issued funded debt, (2) actually outstanding funded debt, and (3) nominally outstanding funded debt. (Note instruction 3-C-Q-R.)

(C) The amounts included herein shall be further divided so as to show the amounts of each class of funded debt as follows:

(1) *Mortgage bonds.*—Bonds secured by lien on physical property and not includible in the other subdivisions of this account.

(2) *Collateral trust bonds.*—Bonds and notes secured by a lien on securities or other negotiable paper, and stock trust certificates that are similar in character to collateral trust bonds.

(3) *Income bonds.*—Bonds which are a lien on a company's income alone, or bonds which, while being a lien on its property and franchises, can claim payment of interest only in case interest is earned.

(4) *Miscellaneous obligations.*—All funded obligations not provided for by the other subdivisions of this account, including unsecured certificates of indebtedness, debenture bonds, plain bonds,

and other similar obligations maturing more than 1 year from date of issue.

(D) Each of the above classes shall also be divided into subclasses according to differences in mortgage or other lien or security therefor, rate of interest, interest dates, or date of maturity.

NOTE A.—Securities maturing 1 year or less from date of issue shall be included in accounts 158.1 or 158.2, as appropriate, except that where an issue of securities maturing serially over a period of more than 1 year contains short-term obligations, such obligations shall be included as funded debt.

NOTE B.—Matured funded debt shall be included in account 163.

NOTE C.—Investment advances, including those represented by notes (note instruction 3–M), shall be included in account 156 or account 157, as may be appropriate.

154.2. **Funded debt subscribed.**—(A) This account shall include the face amount (note instruction 3–K.1) of funded debt for which legally enforceable subscriptions have been received but for which, at the date of the balance-sheet, evidences of indebtedness have not been issued. A separate subaccount shall be maintained for each class of funded debt.

(B) This account shall be debited and account 154.1, "Funded debt", credited when the total amount of each subscription is received and evidences of indebtedness are issued.

(C) Accrued interest on the evidences of indebtedness issued to subscribers shall be accounted for through the appropriate interest, discount, or premium account. (Note instruction 3–K–U, also account 127.)

155. **Receivers' certificates.**—When any receiver acting under the orders of a court is in possession of the property of the company and under the orders of such court issues evidences of indebtedness chargeable upon such property, the face amount (note instruction 3–K.1) of such evidences of indebtedness shall be credited to this account.

156. **Advances from affiliated companies.**—This account shall include the amount of investment advances (note instruction 3–M) from affiliated companies (note instruction 3–D).

NOTE.—Amounts due affiliated companies which are subject to current settlement shall be included in accounts 158.1 or 159.1, as appropriate.

157. **Other long-term debt.**—This account shall include investment advances (note instruction 3–M) from nonaffiliated companies (note instruction 3–S) and individuals, and other long-term debt not provided for elsewhere.

NOTE.—Amounts due nonaffiliated companies and individuals which are subject to current settlement shall be included in accounts 158.2 or 159.2, as appropriate.

VII. CURRENT LIABILITIES

158.1. **Notes payable to affiliated companies.**—This account shall include the face amount (note instruction 3–K.1) of notes, drafts, and other evidences of indebtedness to affiliated companies (note instruction 3–D) issued or assumed by the company (except interest coupons) which are payable on demand or not more than 1 year from date of issue.

NOTE A.—Exclude from this account notes that are within the definition of account 156.

NOTE B.—The records supporting the entries to this account shall be kept so that the company can furnish complete details as to each note, when it is issued, the consideration received, and when it is payable.

158.2. **Other notes payable.**—This account shall include the face amount (note instruction 3–K.1) of notes, drafts, and other evidences of indebtedness to nonaffiliated companies (note instruction 3–S) and individuals issued or assumed by the company (except interest coupons) which are payable on demand or not more than 1 year from date of issue.

NOTE A.—Obligations any part of which matures more than 1 year from date of issue, notes representing investment advances (note instruction 3–M), and notes payable to affiliated companies shall be included in accounts 154.1, 156, 157, or 158.1, as appropriate.

NOTE B.—All unmatured receivers' certificates, regardless of date of maturity, shall be included in account 155.

159.1. **Accounts payable to affiliated companies.**—(A) This account shall include amounts owed by the company to affiliated companies (note instruction 3–D) on all transactions subject to current settlement. There shall be included herein accounts payable arising from divisions of toll revenues.

(B) In the balance-sheet statement there may be included in this account the net amount payable to companies in favor of each of which there is a net credit balance between this account and account 120.1, "Accounts receivable from affiliated companies."

NOTE.—If items included in this account are not actually paid currently, they shall be transferred to account 156.

159.2. **Other accounts payable.**—(A) This account shall include amounts currently due to nonaffiliated companies (note instruction 3–S) and individuals and not provided for in other accounts, such as those for wages, traffic settlements, material and supplies, repairs to telephone plant, matured rents, and interest payable under monthly settlements on short-term loans, advances, and open accounts.

(B) In the balance-sheet statement there may be included in this account the net amount payable to companies in favor of each of which there is a net credit balance between this account and account 120.2, "Other accounts receivable."

160. **Customers' deposits.**—This account shall include the amount of cash deposited with the company by customers as security for the payment for telephone service.

NOTE.—Advance payments made by prospective customers prior to the establishment of service shall be credited to account 164.

162. **Matured interest and dividends.**—This account shall include the amount of matured and unpaid interest on indebtedness of the company, and receivers' certificates, and the amount of dividends due and payable on capital stock but unpaid, uncalled for, or unclaimed at the date of the balance-sheet.

NOTE.—Interest payable under monthly settlements on short-term loans, advances, and open accounts shall be included in accounts 159.1 or 159.2, as appropriate.

163. **Matured long-term debt.**—This account shall include the amount (including any obligations for premiums) of long-term debt and receivers' certificates matured and unpaid without any specific agreement for extension of maturity, including unpresented bonds drawn for redemption through the operation of sinking and redemption fund agreements.

164. **Advance billing and payments.**—This account shall include the amount of advance billing creditable to revenue accounts in future months; also advance payments made by prospective customers prior to the establishment of service. Amounts included in this account shall be credited to the appropriate revenue accounts in the months in which the service is rendered or cleared from this account as refunds are made.

165. **Other current liabilities.**—This account shall include all liabilities of a current character which are not includible in accounts 158.1 to 164, inclusive.

VIII. ACCRUED LIABILITIES NOT DUE

166. **Taxes accrued.**—This account shall include the amount of unpaid taxes accrued. (Note also instruction 22-B-8 and accounts 305 and 322.)

NOTE.—Taxes paid in advance shall be included in account 130.

167. **Unmatured interest, dividends, and rents accrued.**—(A) This account shall include the amount of interest on indebtedness of the company and receivers' certificates, dividends on capital stock, and rents accrued to the date for which the balance-sheet is made, but not payable until after that date.

(B) This account shall be maintained so as to show separately the amount of interest, of dividends, and of rents accrued to the date of the balance-sheet.

NOTE A.—Matured rents are includible in accounts 159.1 or 159.2, and matured dividends and interest in account 162.

NOTE B.—Interest payable under monthly settlements on short-term loans, advances, and open accounts shall be included in accounts 159.1 or 159.2, as appropriate.

IX. DEFERRED CREDITS AND RESERVES

168. Premium on long-term debt.—This account shall include the total of credit balances in the discount, premium, and debt expense accounts, for all classes of long-term debt having credit balances in these accounts. (Note instruction 15.)

169. Insurance reserve.—(A) To this account shall be credited appropriations of income or surplus specifically made to cover self-carried risks for losses through accident, fire, flood, or other causes.

(B) In case the company elects to carry its own risks for losses through accident, fire, flood, or other causes and provides a reserve, other than provision made in the depreciation reserve, to equalize anticipated losses, the charges to account 668, "Insurance", and other appropriate accounts to cover such risks shall be credited to this account. Such charges and credits shall be upon the basis of rates which fairly cover the risks insured. These rates should be determined according to the company's experience and best estimate as to the hazard covered. A schedule of risks covered by this reserve shall be maintained giving a description of the property or the character of the risks covered.

(C) If the company reinsures with insurance companies risks initially covered in this account, the premiums for such reinsurance shall be charged hereto, and the amounts recovered under such commercial insurance shall be credited hereto.

(D) To the extent that losses and damages sustained are covered by this account, an amount equal thereto shall be charged to this account and credited to the accounts appropriate for the losses and damages sustained.

NOTE.—All losses and damages sustained, including those covered by commercial insurance or by this account, shall be charged in the first instance to the depreciation reserve, construction, repair, accidents and damages, or other appropriate account according to the character of the loss. Insurance recoverable or chargeable to this account on account of losses and damages sustained shall be credited to the account to which the losses and damages are chargeable.

170. Provident reserve.—(A) This account shall include specific appropriations of income or surplus and the amounts contributed by employees or others (whether carried in special trust funds or in the general funds of the company) for pensions, accident and death benefits, savings, relief, hospital, and other provident purposes, when administered by trustees or managers acting for the company.

(B) This account shall include also the amount accrued for pensions through charges to account 672, "Relief and pensions."

Amounts so credited shall, when actually paid to retired employees or paid into a trust fund irrevocably devoted to the payment of pensions, be charged hereto.[1]

171. **Depreciation reserve.**—(A) This account shall be credited with amounts concurrently charged to account 608, "Depreciation", and to clearing accounts for currently accruing depreciation (note instruction 3-J) of telephone plant. (Note also instructions 80, 81, and 82.) It shall also be credited with any amounts which the company may elect to charge to account 413, "Miscellaneous debits to surplus", and transfer to this account with respect to past accrued depreciation not provided for. (Note also instructions 20–B and 21.)

(B) At the time of retirement of depreciable telephone plant, this account shall be charged with the original cost (note instruction 3–S.1) of the property retired plus the cost of removal (except the cost of removal of station apparatus) and shall be credited with the salvage value and insurance recovered, if any. It shall be credited with amounts chargeable to account 138, "Extraordinary maintenance and retirements", as provided in instruction 83. (Note also instruction 25.)

(C) For corporate ledger and balance-sheet purposes this account shall be regarded and treated as a single composite reserve. However, for purposes of analysis, the company shall maintain subsidiary records in which the depreciation reserve is broken down into component parts corresponding to the primary telephone plant accounts which include depreciable telephone plant (note also instruction 82); these subsidiary records shall show the current credits and debits to the reserve in complete detail by such primary plant accounts.

172. **Amortization reserve.**—(A) This account shall be credited with amounts concurrently charged to account 613, "Amortization of intangible property", for the amortization of leaseholds, franchises, and patent rights. (Note also instruction 25-E.)

(B) This account shall be credited with any amounts concurrently charged to account 413, "Miscellaneous debits to surplus", to provide a reserve for the retirement of amounts carried in account 201, "Organization." It shall also be credited with any amounts which this Commission may authorize under a plan to amortize the balance in account 100,4, "Telephone plant acquisition adjustment."

(C) When any leasehold carried in account 211, "Land", or any franchise or patent expires, is relinquished, or otherwise retired from service, this account shall be charged with the amount previously credited hereto with respect to the property going out of service. The original cost (note instruction 3–S.1) of the property so retired less the amount chargeable to this account and less the proceeds realized at retirement shall be included in

the appropriate surplus account. (Note accounts 315 and 174 for depreciation of miscellaneous physical property.)

173. **Employment stabilization reserve.**—(A) This account shall be credited with amounts concurrently charged to account 611, "Employment stabilization." When maintenance work for which provision has been made in this account is performed, this account shall be charged with an amount equal to the cost of such work and concurrently account 611 shall be credited.

(B) This account shall also be credited with amounts concurrently charged to account 672, "Relief and pensions", under provisions of paragraph (F) of that account to provide a reserve for termination allowances or similar benefits to employees of the company when such employees are laid off because of lack of work, also to provide necessary and warranted relief to former employees. When disbursements are made for these purposes they shall be charged to this account.

174. **Other deferred credits.**—(A) This account shall include the amount of all deferred credits not includible in accounts 168 to 173, inclusive, such as credit balances in clearing accounts; estimated uninsured casualty liabilities charged to account 669, "Accidents and damages"; amounts awaiting adjustments between accounts; amounts accrued for depreciation of miscellaneous physical property; and revenue, expense, and income items in suspense. (Note also instruction 6.)

(B) When miscellaneous physical property not previously used in telephone service is disposed of, this account shall be charged with the amount previously credited hereto with respect to such property and the book cost of the property so retired less the amount chargeable to this account and less the value of the salvage recovered or the proceeds from the sale of the property shall be included in the appropriate surplus account. In case the property had been used in telephone service previous to its inclusion in account 103, "Miscellaneous physical property", the amount accrued for depreciation thereon after its retirement from telephone service shall be charged to this account and credited to account 171, "Depreciation reserve", and the accounting for its retirement from account 103 shall be in accordance with that applicable to telephone plant retired. (Note also instruction 25.)

X. Contributions of Telephone Plant

175. **Contributions of telephone plant.**—(A) This account, in accordance with instruction 20–B, shall include the amounts of money or its equivalent contributed directly or indirectly for or in connection with the construction or acquisition of telephone plant. The records shall be kept so that the amount and description of each contribution and from whom received will be readily available.

(B) When the service, in connection with which the contribution was made, is permanently discontinued by the company the amount in this account with respect to that service shall be debited hereto and credited to account 402, "Miscellaneous credits to surplus."

NOTE.—Except as provided in paragraph (B) the amounts of contributions shall be permanently carried in this account.

XI. SURPLUS

180. **Surplus reserved.**—This account shall include all amounts, not provided for elsewhere, reserved from surplus including those reserved by charges to income and surplus, such as appropriations of income or surplus to sinking and other fund reserves and reservations charged to income or surplus with respect to operating revenues subject to possible refund under rate litigations.

181. **Unappropriated surplus.**—(A) An account under this title shall be maintained in the general books of the company. The balance of all surplus primary accounts (400 to 416, inclusive) shall be closed into this account at the end of each calendar year. (Note instruction 40.)

(B) If the balance in this account is a deficit, it shall be shown in red in the balance sheet of the report to this Commission.

TELEPHONE PLANT ACCOUNTS

201. Organization.
202. Franchises.
203. Patent rights.
207. Right of way.
211. Land.
212. Buildings.
221. Central office equipment.
231. Station apparatus.
232. Station installations.
233. Drop and block wires.
234. Private branch exchanges.
235. Booths and special fittings.
241. Pole lines.
242.1. Aerial cable.
242.2. Underground cable.
242.3. Buried cable.
242.4. Submarine cable.
243. Aerial wire.
244. Underground conduit.
261. Furniture and office equipment.
[illegible]4. Vehicles and other work equipment.
276. Telephone plant acquired.
277. Telephone plant sold.

PLANT ACCOUNTS

(Note particularly instructions 20 to 27, inclusive)

201. Organization.—This account shall include the cost of organizing and incorporating the company. (Note also instructions 14 and 15.)

ITEMS

[Note instruction 8]

Amounts paid for legal services.
Amounts paid for privileges of incorporation.
Office expenses incident to organizing the company.
Special counsel and other fees and expenses in mergers, consolidations and reorganizations.

NOTE A.—This account shall not include any discounts on securities issued, nor shall it include costs incident to negotiating loans, selling bonds

or other evidences of debt, or expenses in connection with the authorization, issuance, sale or resale of capital stock.

NOTE B.—Exclude from this account and include in account 664 the cost of preparing and filing papers in connection with the extension of the term of incorporation unless the first organization costs have been written off.

NOTE C.—When charges are made to this account for expenses incurred in mergers, consolidations, or reorganizations, amounts previously included in this account on the books of the various companies concerned shall not be carried over.

202. **Franchises.**—This account shall include the original cost (note instruction 3–S.1) of governmental franchises and similar rights running for more than 1 year which are necessary in the conduct of the company's telephone operations. It shall include amounts paid in cash and the cost of plant, material, supplies, and equipment given as the initial consideration for such franchises; cost of advertising, governmental election costs assumed by the company, and similar expenses incurred in procuring such franchises; also the original cost of franchises acquired by assignment. This account shall include amounts, other than those includible in account 201, "Organization", paid to municipalities or other governmental agencies as a condition precedent to engaging in business, whether or not the right to occupy city property, streets, and highways is obtained in connection therewith. (Note also instruction 22–B–7.)

NOTE A.—The cost of franchises running for 1 year or less after acquisition shall be charged to account 673, or, if such franchises extend beyond the current year, to account 133. Franchises acquired at small cost may be charged to account 673 irrespective of their term of life.

NOTE B.—Franchise taxes (payable annually or more frequently) shall be charged to account 305.

NOTE C.—This account shall not include the cost of plant, material and supplies, or equipment furnished to municipalities or other governmental authorities when given other than as initial consideration for franchises or similar rights. (Note also account 673.)

203. **Patent rights.**—This account shall include the original cost (note instruction 3–S.1) of patent rights having a life of more than 1 year from date of acquisition for use in connection with the company's telephone operations.

NOTE.—The cost of patents having an estimated service life of 1 year or less and patents acquired at small cost shall be charged to account 675.

207. **Right of way.**—This account shall include the original cost (note instruction 3–S.1) of land, and of leaseholds, easements, and similar rights in land having a term of more than 1 year, acquired for the location of pole line, cable, wire, and conduit plant, also the cost of permits to erect poles and to place conduit when the expected period of occupancy under such permits exceeds the estimated life of the initial plant installed. It shall include

the related portion of the pay and expenses of right of way agents and other costs of acquiring such land, rights, and permits.

NOTE A.—The cost of permits to erect poles and to place conduit when the expected period of occupancy under such permits does not exceed the estimated life of the initial plant installed, also the cost of other permits not includible in this account, such as those to place cable and wire on buildings and fences, and the related pay and expenses of employees and other costs incident to acquiring such permits shall be included in the account appropriate for the cost of the property constructed. (Note also instruction 22–B–7.)

NOTE B.—Annual or more frequent payments for the use of right of way shall be charged to account 671.

NOTE C.—Payments to municipalities or other governmental agencies (exclusive of franchise taxes) as consideration for a franchise or right to conduct the company's telephone operations, whether or not the right to occupy city property, streets, and highways is obtained thereunder, shall be accounted for as franchise payments. (Note also accounts 202 and 673.)

211. Land.—(A) This account shall include the original cost (note instruction 3–S.1) of land and of leaseholds, easements, and similar rights in land having a term of more than 1 year used for general and central office buildings, garages, shops, and for storage and other telephone purposes other than right of way. It shall also include special assessments upon lands for the construction of public improvements. (Note also instruction 25–C.)

(B) When land, together with buildings thereon, is acquired the original cost shall be fairly apportioned between the land and the buildings and accounted for accordingly. If the plan of acquisition contemplates the removal of the buildings, the total cost of the land and buildings shall be accounted for as the cost of the land, and the salvage value of the buildings when disposed of shall be deducted from the cost of the land so determined. (See also note E to this account.)

ITEMS

[Note instruction 8]

Assessments for the construction of public improvements. (See also note D to this account.)
Clearing or defending title against claims relating to period prior to purchase.
Commissions and fees to brokers, agents, and others.
Condemnation proceedings, including court costs and special counsel fees.
Conveyancer and notarial fees.
Examination and registration of titles.
Grading of land not in connection with buildings.
Relocating property of others in acquisition of land.
Sidewalks on public streets abutting company's property.
Taxes assumed, accrued prior to date of acquisition.

Taxes on land during the period of construction. (Note also instruction 22–B–8.)
Voiding leases to secure possession of land acquired.

NOTE A.—Annual or more frequent payments for the use of land shall be charged to the account appropriate for rents.

NOTE B.—When land is acquired for which there is not a definite plan for its use in telephone service, its cost shall be charged to account 103.

NOTE C.—When land is acquired in excess of that required for telephone purposes, the cost of such excess land shall be included in account 103.

NOTE D.—Installments of assessments for public improvements, including interest, if any, which are deferred without option to the company shall be included in this account only as they become due and payable. Interest on assessments which are not paid when due shall be included in account 336.

NOTE E.—In case land is purchased for immediate use in a construction project, its cost shall be included in account 100.2 until such time as the project involved is completed ready for service.

212. **Buildings.**—(A) This account shall include the original cost (note instruction 3–S.1) of buildings, and the cost of all permanent fixtures, machinery, appurtenances, and appliances installed as a part thereof. It shall include costs incident to the construction or purchase of a building and to securing possession and title.

(B) When land, together with the buildings thereon, is acquired the original cost shall be fairly apportioned between the land and buildings, and the amount applicable to the buildings shall be included in this account; the amount applicable to the land shall be included in account 211. (Note also account 211.)

ITEMS

[Note instruction 8]

Awnings.
Boilers, furnaces, fixtures, and machinery for heating, lighting, ventilating, and plumbing.
Cable vaults and conduits constructed as part of the building.
Commissions and fees to brokers, agents, architects, and others.
Door checks and door stops.
Drainage and sewerage systems.
Electric wiring.
Elevators.
Fences and hedges.
Fire-extinguisher systems.
Garages, shops, and stables.
General and central office buildings.
Grading, excavating, and preparing grounds for buildings, including laying out of grounds after construction.
Improvements to leased buildings. (Note also instruction 23.)
Linoleum and similar floor covering, excluding carpets and rugs.
Motors and generators.
Partitions, including movable.
Piers and foundations for machinery constructed as a permanent part of a building.

Platforms, storage or loading.
Power boards.
Refrigeration systems.
Retaining walls.
Screens, door and window.
Sheds.
Sidewalks, pavements and driveways on building grounds.
Sprinkling systems.
Storm doors and windows.
Voiding leases to secure possession of buildings acquired.
Water, steam, and gas pipes.
Water-supply systems.
Window shades and ventilators.

NOTE A.—This account shall not include the cost of any telephone equipment or wiring or apparatus for generating or controlling electricity for operation of the telephone system.

NOTE B.—The cost of submarine cable terminal huts shall be included in account 242.4.

221. Central office equipment.—(A) This account shall include the original cost (note instruction 3–S.1) of electrical instruments, apparatus, and equipment, other than station equipment, in central offices (including terminal and test rooms), repeater stations and test stations used in transmitting traffic and operating signals, and similar equipment in operators' schools and other centralized locations.

(B) This account shall also include the original cost of operators' chairs, wire chiefs' tools, desks and tables equipped with central office telephone equipment, and other furniture, fixtures, and equipment designed specifically for use in central offices, repeater stations, etc., or installed as a part of the electrical equipment therein. (See also note A to this account.)

ITEMS

[Note instruction 8]

Aisle—lighting equipment.
Balconies for distributing frames.
Banks—connector, selector.
Batteries.
Battery cabinets.
Boards—floor alarm, power, test, service observing.
Building alterations, minor, such as opening and closing holes in ceilings, partitions, walls, and floors to permit installations of equipment, power conduit, and wiring.
Cables. (See also note B to this account.)
Calculagraphs.
Call registers.
Carrier—current equipment.
Carrier line filters.
Circuit breakers.
Covers for transmission power apparatus.
Desks and tables when equipped with central office telephone equipment. (See also note A to this account.)
Engines, including special foundations not a part of buildings.

Frames—alarm, connector, decoder, decoder connector, line finder, line switch, repeater, selector, sender, test.
Fuse boards.
Fuse panels.
Generators, including special foundations not a part of buildings.
Jumper wires.
Key indicator equipment.
Line filters.
Loading coils. (See also note C to this account.)
Loudspeaker equipment.
Main and intermediate frames.
Meters.
Motors, including special foundations not a part of buildings.
Multiplex apparatus.
Operators' breastplate transmitters.
Operators' chairs.
Operators' head sets.
Platforms, not part of buildings.
Pole changers.
Power circuits for emergency use including payment for installation by others of circuits not owned.
Power plants.
Power panels.
Protectors.
Pulse machines and tone machines.
Radio transmitting and receiving equipment.
Rectifiers.
Relay racks and coil racks.
Relays.
Register cabinets.
Repeater sets.
Rheostats.
Ringing machines, including special foundations not a part of buildings.
Rolling ladders.
Switchboards and other electrical equipment used in operators' schools.
Switchboards—subscribers' "A" and "B" trunk, toll, dial system.
Switches—connector, line repeater, selector, repeater, test, distributor.
Tarpaulins.
Telegraph instruments and equipment.
Telephotographic equipment.
Teletypewriter switchboards and equipment.
Test boards.
Testing and routining central office equipment prior to assignment to service.
Test tables.
Testing equipment and tools, central office. (See also note D to this account.)
Ticket holders.
Toll ticket carriers.
Turrets.
Water stills for battery service.

NOTE A.—The cost of desks and tables not equipped with central office equipment, and of kitchen and dining room equipment, chairs of the same types as used in other offices, typewriters, portable electric fans, etc., shall be charged to account 261.

NOTE B.—The cost of cables leading from the main frame to outside plant shall be included in the plant account appropriate for the cost of cables with which they connect.

NOTE C.—The cost of loading coils on circuits leading from the main frame to outside plant shall be included in the account charged with the cost of the circuit of which they are a part.

NOTE D.—The cost of portable testing equipment and tools other than those regularly used in central offices shall be charged to account 264.

231. **Station apparatus.**—This account shall include the original cost (note instruction 3–S.1) of station apparatus, installed either for customers' or the company's use, excluding the cost of installation and inside wires.

ITEMS

[Note instruction 8]

Backboards.
Batteries, station.
Battery boxes.
Bell boxes.
Coin collectors.
Cords.
Desk sets, hand sets, and wall sets, including those used at main, extension, private branch exchange, and private line stations, etc. This includes such sets as operators' sets at private branch exchanges, order turrets and order tables, and those used in central offices and operators' schools. (See also note A to this account.)
Dials.
Extension bells.
Hand-set mountings.
Induction coils.
Messenger, and similar signaling devices.
Printer-telegraph equipment.
Program-supply equipment.
Public-address equipment.
Receivers.
Signal cases.
Station switching and signaling devices, including apparatus cabinets, keys, key cabinets, and devices used with intercommunicating systems.
Telegraph equipment.
Teletypewriter equipment.
Transmitters.

NOTE A.—Operators' head sets and breastplate transmitters in central offices and at private branch exchanges and test sets such as those used by wire chiefs, linemen, and others, shall be included in accounts 221, 234, and 264, as appropriate.

NOTE B.—The cost of station protectors is includible in account 232.

232. **Station installations.**—(A) This account shall include the original cost (note instruction 3–S.1) of installing station apparatus and of inside wires. Inside wires include:

(1) The wires (or small cables) from the station apparatus to the point near the entrance to the building where the drop or

block wire or cable terminates, or to the junction boxes where the house cable or other cable terminates.

(2) The wires (or small cables) used to connect station apparatus in the same building, such as main stations with extension stations, and stations of intercommunicating systems.

(3) The wires (or small cables) used to connect private branch exchange switchboards or their distributing frames with terminal stations located in the same building.

(B) This account shall include the cost of clamps, cleats, connecting blocks, ground wires, ground rods, nails, station protectors, screws, and other material used in the installation of station apparatus and inside wires.

NOTE A.—Costs chargeable to this account in connection with cables are restricted to small cables used in station installations instead of wires, such as those run from wall outlets or floor terminals to the station apparatus. The cost of other inside cables, including riser and distributing cables in buildings, which by their physical character, method of installation, and permanence constitute house cables, is chargeable to account 242.1.

NOTE B.—The cost of inside wires (or small cables) installed specifically to serve as trunk, battery, or generator circuits from a private branch exchange to the point of connection with the permanent house or outside cables or wires shall be charged to account 234.

233. **Drop and block wires.**—(A) This account shall include the original cost (note instruction 3–S.1) of drop and block wires or service connections, i. e., the portion of a customer's circuit (whether aerial or underground) extending from the inside wire (usually at the station protector or connecting block) or from the station equipment when no inside wire is involved, to the point of connection with the general overhead or underground system. This includes such circuit, carried by means of wire or small cables, extending to the cable terminal in cases where connection is made with a general cable system, or to the point of connection with the aerial wire plant in cases where connection is made with a general wire system. The company shall exercise such precautions as are necessary to prevent credits to this account for aerial wire removed.

(B) This account shall also include the original cost of brackets, bridle rings, insulators, knobs, span clamps, screws, sleeves, strand, tubes, and other material used in the installation of drop and block wires; the cost of trimming trees and other costs incurred in the installation of such wires; the cost of pipes or other protective covering for underground service connections; and the cost of permits and privileges for construction.

234. **Private branch exchanges.**—This account shall include the original cost (note instruction 3–S.1) of private branch exchange equipment installed either for customers' or the company's use.

ITEMS

[Note instruction 8]

Attendants' cabinets or cordless switchboards.
Cable or wires from distributing frame to switchboard.
Code call units.
Code sending sets.
Dial system branch exchanges.
Distributing frames.
Inside wires (or small cables used instead of wires) installed specifically to serve as trunk, generator, or battery circuits from a private branch exchange to the point of connection with the permanent house or outside cables or wires.
Operators' chairs.
Operators' head sets and breastplate transmitters.
Order receiving tables.
Order turrets.
Power equipment, including special foundations.
Protectors.
Switchboards.

NOTE A.—The cost of riser and distributing cables in buildings other than central offices, which by their physical characteristics, method of installation, and permanence constitute regular house cables shall be charged to account 242.1.

NOTE B.—The cost of poles, wires, and cables, whether or not on private property, used to connect the private branch exchange with the terminal stations shall be charged to the pole, wire, and cable accounts.

NOTE C.—The cost of cross-connection boxes installed as a part of the house cable system, including those used as the distributing frames for private branch exchanges, shall be charged to account 242.1.

235. **Booths and special fittings.**—This account shall include the original cost (note instruction 3–S.1) of telephone booths and special fittings (exclusive of station apparatus) such as attendants' desks (including equipment or switchboards), counters, railings, chairs, fans, cash registers, directory tables, stands or shelves, and public telephone signs.

241. **Pole lines.**—This account shall include the original cost (note instruction 3–S.1) of poles, crossarms, guys, and other material used in the construction of pole lines.

ITEMS

[Note instruction 8]

Anchors.
A and H fixtures.
Bolts.
Braces, pole and back.
Bridge fixtures.
Cable arms.
Clearing routes and tree trimming except maintenance of previous clearings. (Note also account 602.1.)
Crossarms.
Extension arms.
Guard arms.
Guy clamps.

Guy stubs.
Guy wire or strand.
Painting, treating, gaining, roofing, shaving, and stenciling poles.
Permits and privileges for construction. (Note also account 207 and instruction 22–B–7.)
Pins.
Pole brackets, wooden.
Poles.
Pole steps.
River crossing and long span fixtures.
Strain insulators.
Towers.

242.1. **Aerial cable.**—This account shall include the original cost (note instruction 3–S.1) of aerial cable and other material used in the construction of such cable.

ITEMS

[Note instruction 8]

Bonds and grounds.
Cable—block, feeder, main, subsidiary.
Cable—house, including riser and distributing cables extending to floor terminal boxes, cross-connection boxes at wall outlets, etc., where connection is made with inside wires.
Cable clamps.
Cable rings.
Cable terminals or boxes.
Cross-connection wires and fuses installed in the first equipment for service of cable terminals or boxes.
Floor terminal boxes and cross-connection boxes at wall outlets.
Fuse boxes.
Loading coils, building-out condensers, carrier-line filters, and cases therefor.
Main-frame-terminating cable extending to outside cable.
Negative returns.
Permits and privileges for construction. (Note also account 207.)
Pole seats and balconies.
Pressure contactor-terminals.
Protectors and arresters.
Safety straps.
Sleeves.
Strand, suspension.
Tree guards.
Trolley guards.

NOTE A.—House cables are considered to be extensions of aerial cable plant. They do not include the inside wires extending from terminal boxes of house cables to subscribers' stations which are included in account 232, or the cables for subscribers' private branch exchange switchboards which are included in account 234.

NOTE B.—The company's records shall be kept so that the miles of wire in aerial cable may be shown in the annual reports to this Commission.

242.2. **Underground cable.**[1]—This account shall include the original cost (note instruction 3–S.1) of underground cable and other material used in the construction of such cable.

[1] In conduit.

ITEMS

[Note instruction 8]

Bonds and grounds.
Cable—feeder, main, subsidiary.
Cable terminals or boxes.
Cross-connection wires and fuses installed in the first equipment for service of cable terminals or boxes.
Electrolysis surveys made in the course of installing cable.
Fuse boxes.
Loading coils, building-out condensers, carrier-line filters, and cases therefor.
Main-frame-terminating cable extending to outside cable.
Negative returns.
Permits and privileges for construction. (Note also account 207.)
Pressure contactor-terminals.
Protectors and arresters.
Pumping out and cleaning manholes and ducts in underground cable construction work. (See also note A to this account.)
Sleeves.
Splicing boxes.
Strand, suspension.

NOTE A.—The cost of pumping water out of manholes and of cleaning manholes and ducts in connection with the maintenance or operation of telephone plant shall be charged to accounts 602.3 or 602.4, as appropriate.

NOTE B.—The cost of small cables used in station installations instead of wires, such as those run from wall outlets or floor terminals to the station apparatus, shall be charged to account 232. The cost of small cables used as drop wires shall be included in account 233.

NOTE C.—The cost of cable leading from central office main frames to other central office equipment shall be charged to account 221.

NOTE D.—House cables are considered to be extensions of aerial cable plant. They do not include the inside wires extending from terminal boxes of house cables to subscribers' stations which are included in account 232, or the cables for subscribers' private branch exchange switchboards which are included in account 234.

NOTE E.—The company's records shall be kept so that the miles of wire in underground cable may be shown in the annual reports to this Commission.

242.3. **Buried cable.**—This account shall include the original cost (note instruction 3–S.1) of buried cable and other material used in the construction of such cable.

ITEMS

[Note instruction 8]

Cable—feeder, main.
Cable terminals or boxes.
Cross-connection wires and fuses installed in the first equipment for service of cable terminals or boxes.
Loading coils, building-out condensers, carrier-line filters, and cases therefor.
Main-frame-terminating cable extending to outside cable.
Negative returns.
Permits and privileges for construction. (Note also account 207.)
Pressure contactor-terminals.

Protective covering for buried cable, i. e., cable not run in regular conduit, such as fiber or other material (except when constructed so as to be reusable in place for other cable) and the cost of manholes, etc., designed specifically for use in such construction.
Protectors and arresters.
Pumping out and cleaning manholes in buried cable construction work. (See also note A to this account.)
Sleeves.
Splicing boxes.
Trenching for and burying cable not run in regular conduit.

NOTE A.—The cost of pumping water out of manholes and of cleaning manholes and ducts in connection with the maintenance or operation of telephone plant shall be charged to accounts 602.3 or 602.4, as appropriate.

NOTE B.—The company's records shall be kept so that the miles of wire in buried cable may be shown in the annual reports to this Commission.

242.4. **Submarine cable.**—This account shall include the original cost (note instruction 3-S.1) of submarine cable and other material used in the construction of such cable.

ITEMS

[Note instruction 8]

Cable—feeder, main.
Cable terminals or boxes.
Loading coils, building-out condensers, carrier-line filters, and cases therefor.
Permits and privileges for construction. (Note also account 207.)
Pressure contactor-terminals.
Protectors and arresters.
Sleeves.
Submarine cable terminal huts.

NOTE.—The company's records shall be kept so that the miles of wire in submarine cable may be shown in the annual reports to this Commission.

243. **Aerial wire.**—This account shall include the original cost (note instruction 3-S.1) of aerial wire other than drop and block wires, including insulators, tie wires, and other material used in the construction of aerial wire plant. The company shall exercise such precautions as are necessary to prevent credits to this account for drop and block wires removed.

ITEMS

[Note instruction 8]

Bridle rings.
Bridle wire.
Ground wire, clamps, and rods.
Insulators and thimbles.
Loading coils, building-out condensers, carrier-line filters, and cases therefor.
Permits and privileges for construction. (Note also account 207.)
Protectors and arresters.
Repeating coils.
Tie wires.
Transposition brackets.

Transposition of the circuits in initial construction work and any additions or betterments resulting from transposing or retransposing existing circuits.

NOTE.—The cost of drop and block wires shall be included in account 233.

244. **Underground conduit.**—This account shall include the original cost (note instruction 3–S.1) of the, pipe, and other conduit, whether underground, in tunnels or on bridges, and of manholes, handholes, and service boxes, including cable racks and other furnishings thereof, and the cost of riser pipe. It shall include the cost of opening trench and repaving in the construction of such plant and the cost of permits and privileges for construction. (Note also account 207.)

NOTE A.—The cost of protective covering for buried cable, i. e., cable not run in regular conduit, such as fiber or other material (except when constructed so as to be reusable in place for other cable) and the cost of trenching, manholes, etc., designed specifically for use in such construction shall be charged to account 242.3.

NOTE B.—The cost of pipes or other protective covering for underground drop and block wires or service connections shall be included in account 233.

261. **Furniture and office equipment.**—This account shall include the original cost (note instruction 3–S.1) not provided for in other accounts, of furniture and equipment in offices, storerooms, shops, and other quarters. (Note also accounts 221, 234, and 235 and instruction 20–D.)

ITEMS

[Note Instructions 8]

Beds, cots, and couches.
Bins, counters, and shelves.
Bookcases.
Cabinets and filing cases.
Cages, cashiers'.
Chairs, carpets, and rugs.
Clocks.
Davenports.
Desks.
Equipment in rest, dining, recreation, and medical rooms.
Fans, electric, portable.
Fire extinguisher equipment, portable.
Floor scrubbing and polishing machines.
Gas and electric fixtures, portable.
Lockers and wardrobes, portable.
Mirrors, portable.
Motion-picture equipment.
Office devices, including addressing, billing, blueprinting, computing, dating, duplicating, mailing, photostat and recording machines, cash registers, check writers, postage meter machines, typewriters, etc.
Pianos and phonographs.
Radio sets.
Racks—magazine, newspaper, umbrella, and clothing.
Refrigerators, portable.

Safes.
Sewing machines.
Stoves.
Switchboards, special type public demonstration.
Tables.
Vacuum sweepers.
Vending machines.
Water coolers.

NOTE.—The cost of fixtures attached to and constituting a part of buildings shall be charged to account 212.

264. **Vehicles and other work equipment.**—This account shall include the original cost (note instruction 3–S.1) of vehicles, tools, garage and shop machinery and equipment, and miscellaneous work equipment not provided for in other accounts. (Note also instruction 20–D.)

ITEMS

[Note instruction 8]

Air compressors.
Automobiles, motor trucks and tractors, including those equipped with earth-boring machines, pumps, winches, etc.
Blowers, power.
Carts, cable splicers'.
Camp wagons, cars, and mounted kitchens.
Compressed air tools.
Concrete mixers and breakers.
Derricks.
Draft animals.
Drills and hammers, power.
Earth-boring machines.
Forges.
Gasoline and oil pumps, portable.
Hand tools.
Hand trucks.
Harness.
Lathes.
Loaders, power.
Motorboats and barges.
Motorcycles and bicycles.
Motors and generators.
Planers.
Pole-treating apparatus, chemical.
Pumps.
Tamping and back filling machines.
Tents, cable splicers'.
Testing equipment, portable. (See also note B to this account.)
Torches.
Trailers.
Trenching machines.
Wagons.
Winches, power.
Wire-measuring machines.

NOTE A.—The cost of chairs, desks, tables, etc., in garages and shops shall be charged to account 261.

NOTE B.—The cost of testing equipment and tools regularly used in central offices shall be charged to account 221.

276. **Telephone plant acquired.**—This account shall be charged temporarily with the cost of acquisition (i. e., amount of money actually paid or the current money value of any consideration other than money exchanged for telephone plant, together with the preliminary expenses incurred in connection with the acquisition) of telephone plant pending distribution to the primary telephone plant accounts and to other accounts. (Note also instructions 21 and 82.)

277. **Telephone plant sold.**—This account shall be credited temporarily with the original cost (note instruction 3–S.1) at the time of retirement of telephone plant sold pending determination of the amounts to be credited to the primary telephone plant accounts. (Note also instruction 25–F.)

NOTE.—In connection with completing the accounting for telephone plant sold, appropriate adjustments shall be made with respect to any related depreciation accruals.

INCOME STATEMENT

I. Telephone Operating Income

Item		
1.	300.	Operating revenues.
2	301.	Operating expenses.
3.		Net operating revenues (item 1 less item 2).
4.	302.	Rent from lease of operating property.
5.	303.	Rent for lease of operating property.
6.	305.	Operating taxes.
7.		Net operating income (items 3 and 4 less items 5 and 6).

II. Other Income

8.	312.	Dividend income.
9.	313.	Interest income.
10.	314.	Income from sinking and other funds.
11.	315.	Incomes from miscellaneous physical property.
12.	316.	Miscellaneous income.
13.		Total other income (the sum of items 8 to 12, inclusive).

III. Miscellaneous Deductions from Income

14.	32[illegible].	Miscellaneous taxes.
15.	323.	Miscellaneous income charges.
16.		Total miscellaneous deductions (the sum of items 14 and 15).
17.		Income available for fixed charges (items 7 and 13 less item 16).

IV. Fixed Charges

18.	335.	Interest on funded debt.
19.	336.	Other interest deductions.
20.	338.	Amortization of discount on long-term debt.
21.	339.	Release of premium on long-term debt—Cr.
22.	340.	Other fixed charges.
23.		Total fixed charges (the sum of items 18 to 22, inclusive).
24.		Income after fixed charges (item 17 less item 23).

V. Contingent Interest

25.	341.	Contingent interest on funded debt.
26.		Net income (net profit) (item 24 less item 25).

VI. Disposition of Net Income

27. 342. Contractual reservations of income.
28. 343. Miscellaneous reservations of income.
29. 344. Dividend appropriations of income.
30. Total reservations and appropriations (the sum of items 27 to 29, inclusive).
31. 400. Income balance (item 26 less item 30).

INCOME ACCOUNTS

(Note particularly instructions 30 and 31)

I. Telephone Operating Income

300. **Operating revenues.**—This account shall include the total revenues for the accounting period which are provided for in the operating revenue accounts 500 to 530, inclusive. (Note also instruction 2–C.)

301. **Operating expenses.**—This account shall include the total expenses for the accounting period which are provided for in the operating expense accounts 602.1 to 677, inclusive. (Note also instruction 2–C.)

302. **Rent from lease of operating property.**—(A) This account shall include rents from the exclusive use of telephone operating property held as a whole and operated by others, such as a complete telephone plant, a complete exchange, or a complete toll system.

(B) Rents are creditable to this account whether receivable in cash or disbursed by the lessee in behalf of the company as taxes on the rented property, interest on funded debt, guaranteed dividends on stock, or otherwise.

Note.—The rent from property the cost of which is includible in account 103 shall be included in account 315.

303. **Rent for lease of operating property.**—(A) This account shall include rents for the exclusive use of telephone operating property held as a whole and operated by the company, such as a complete telephone plant, a complete exchange, or a complete toll system.

(B) This account shall include also taxes borne by the lessee of property, the rent for which is chargeable to this account.

(C) Rents are chargeable to this account whether payable in cash or disbursed by the lessee in behalf of the lessor as taxes on the rented property, interest on funded debt, guaranteed dividends on stock, or otherwise.

Note A.—If leased telephone plant the rent for which is chargeable to this account is sublet to others, the rent receivable therefrom shall be

credited to the account appropriate for rent from owned property of the same class.

NOTE B.—Rents payable for property used by the company for other than telephone operations shall be included in account 315.

NOTE C.—Charges for depreciation of telephone operating property leased as a whole and operated by the company shall be included in account 608 or clearing accounts, as appropriate, on the same basis as for owned property (note also instruction 81) when the company is responsible for depreciation under the terms of the lease.

305. **Operating taxes.**—(A) This account shall include all Federal, State, county, municipal, and other taxing-district taxes, including franchise taxes payable annually or more frequently, relating to telephone plant, operations, and privileges for the period for which the income account is stated. Taxes accrued through this account prior to their payment shall be credited to account 166, "Taxes accrued." (Note also instruction 22–B–8.)

(B) Taxes on leased telephone plant shall be included in this account by the owner. Any taxes on rented telephone plant which are borne by the lessee shall be appropriately credited by the owner to account 524, "Rent revenues", or account 302, "Rent from lease of operating property", and charged by the lessee to account 671, "Operating rents", or account 303, "Rent for lease of operating property."

NOTE A.—Taxes other than those on telephone plant, operations, and privileges shall be charged to accounts 100.3 or 322, as appropriate. (Note also instruction 22–B–8.)

NOTE B.—Special assessments for street and other improvements and special benefit taxes, such as water taxes and the like, shall be included in the operating expense accounts or investment accounts, as may be appropriate.

NOTE C.—Discounts allowed for prompt payment of taxes shall be credited to the account to which the taxes are chargeable.

NOTE D.—Interest on tax assessments which are not paid when due shall be included in account 336.

NOTE E.—The accounting for taxes on physical property during construction and before the facilities are completed ready for service, and taxes on property held for future telephone use shall be in accordance with instruction 22–B–8.

NOTE F.—Taxes paid by the company under tax-free covenants on indebtedness shall be charged to account 340.

II. OTHER INCOME

312. **Dividend income.**—(A) This account shall include dividends on stock, the income from which is the property of the company, whether such stock is owned by the company and held in its treasury, or deposited in trust (except in sinking or other funds, see note B to this account), or controlled through lease, or otherwise.

(B) Dividends shall not be credited to this account before actual collection, unless their payment is reasonably assured by past experience, guaranty, anticipated provisions, or otherwise.

NOTE A.—These accounts shall not include dividends or other returns on securities issued or assumed by the company and held by or for it, whether pledged as collateral, or held in its treasury, in special deposits, or in sinking or other funds.

NOTE B.—Dividends on stocks of other companies held in sinking or other funds shall be credited to account 314.

313. Interest income.—(A) This account shall include interest on securities, including notes and other evidences of indebtedness, the income from which is the property of the company, whether such securities are owned by the company and held in its treasury, or deposited in trust (except in sinking or other funds, see note B to this account), or controlled through lease, or otherwise. It shall include also interest on bank balances, certificates of deposits, open accounts, and other analogous items.

(B) Interest shall not be credited to this account before actual collection, unless its payment is reasonably assured by past experience, guaranty, anticipated provisions, or otherwise.

(C) This account shall be credited with such amounts as are charged to the telephone plant accounts for interest on funds expended for construction purposes, as provided in instruction 22–B–10.

(D) There may be included in this account for each month the applicable amount requisite to extinguish, during the interval between the date of acquisition and date of maturity, the difference between the purchase price and the par value of securities owned, the income from which is includible in this account. Amounts thus credited or charged shall be concurrently included in the accounts in which the securities are carried. Any such difference remaining unextinguished at the sale or upon the maturity and satisfaction of such securities shall be cleared to account 413, "Miscellaneous debits to surplus", or account 402, "Miscellaneous credits to surplus."

NOTE A.—These accounts shall not include interest or other returns on securities issued or assumed by the company and held by or for it, whether pledged as collateral, or held in its treasury, in special deposits, or in sinking or other funds.

NOTE B.—Interest on cash and on securities issued by others shall be included in account 314 when such assets are held in sinking or other funds.

NOTE C.—Cash discounts on bills for material purchased shall not be included in this account. (Note also account 122.)

314. Income from sinking and other funds.—(A) This account shall include the income accrued on cash, securities issued by other

companies, and other assets (not including securities issued or assumed by the company) held in sinking and other funds.

(B) There may be included in this account for each month the applicable amount requisite to extinguish, during the interval between the date of acquisition and the date of maturity, the difference between the purchase price and the par value of securities held in sinking or other funds. Amounts thus credited or charged shall be concurrently included in the accounts in which the securities are carried. Any such difference remaining unextinguished upon the maturity and satisfaction of such securities shall be cleared to account 413, "Miscellaneous debits to surplus", or account 402, "Miscellaneous credits to surplus."

NOTE.—Income from sinking and other funds required to be held in such funds, and credits to reserve accounts representing income from funds, shall be accounted for as provided in instruction 31.

315. **Income from miscellaneous physical property.**—This account shall include the net balance of the revenues from and the expenses (including depreciation and insurance) of physical property the cost of which is includible in account 103, "Miscellaneous physical property", and also of physical property of others leased and used by the company for other than telephone operations. The rent for leased property which is used by the company for other than telephone operations, assessments when borne by the company for maintenance of public improvements against property the cost of which is includible in account 103, and directly assignable administration expenses incident to operation of miscellaneous physical property, shall be included in this account.

NOTE A.—Net credit balances shall be shown in the income statement of the report to this Commission in black and net debit balances in red.

NOTE B.—Taxes on miscellaneous physical property shall be included in account 322.

316. **Miscellaneous income.**—This account shall include all items, not provided for elsewhere, properly creditable to income.

ITEMS TO BE CREDITED

[Note instruction 8]

Fees collected in connection with the exchange of coupon bonds for registered bonds.

Profits from the telephone operations of other companies realized by the company under contracts.

Profits realized from custom work performed for others not incident to the company's telephone operations.

III. MISCELLANEOUS DEDUCTIONS FROM INCOME

322. **Miscellaneous taxes.**—This account shall include all taxes not provided for elsewhere, such as taxes on miscellaneous physi-

cal property. (Note also instruction 22–B–8.) Taxes accrued through this account prior to their payment shall be credited to account 166, "Taxes accrued."

NOTE A.—Special assessments for street and other improvements and special benefit taxes, such as water taxes and the like, shall be included in the operating expense accounts or investment accounts, as may be appropriate.

NOTE B.—Discounts allowed for the prompt payment of taxes shall be credited to the account to which the taxes are chargeable.

NOTE C.—Interest on tax assessments which are not paid when due shall be included in account 336.

323. **Miscellaneous income charges.**—This account shall include all items not provided for elsewhere properly chargeable to income.

ITEMS TO BE CHARGED

[Note instruction 8]

Contributions for charitable or social or community welfare purposes.
Current expenses of trustees in maintaining and administering trusts incident to outstanding debt of the company.
Membership fees and dues in associations, other than those of the company itself in associations of telephone companies and of employees in professional organizations.
Uncollectible amounts previously credited to accounts 312 to 316, inclusive. (See also instruction 11 and note to account 530.)

IV. FIXED CHARGES

335. **Interest on funded debt.**—(A) This account shall include the current accruals of interest on all classes of debt the principal of which is includible in account 154.1, "Funded debt", and account 155, "Receivers' certificates", except interest provided for in account 341, "Contingent interest on funded debt." (Note also instruction 22–B–10.) It shall also include the interest on funded debt the maturity of which has been extended by specific agreement.

(B) This account shall be kept so that the interest on each class of funded debt and on receivers' certificates may be shown separately in the annual reports to this Commission.

NOTE A.—These accounts shall not include charges for interest on funded debt issued or assumed by the company and held by or for it, whether pledged as collateral or held in its treasury, in special deposits, or in sinking or other funds.

NOTE B.—Interest expressly provided for and included in the face amount of securities issued shall be charged at the time of issuance to account 133 and cleared to this account as the term expires to which the interest applies.

336. **Other interest deductions.**—(A) This account shall include all interest deductions not provided for elsewhere. Dis-

count, premium, and expense on notes maturing 1 year or less from date of issue shall be included in this account in equal monthly installments throughout the term of the notes or included herein at the time such notes are issued. (Note also instruction 22–B–10.)

(B) A list of representative items of indebtedness follows, the interest on which is chargeable to this account (note instruction 8):

Advances from affiliated companies. (Note also account 156.)
Advances from nonaffiliated companies and other liabilities included in account 157.
Assessments for public improvements past due.
Bond coupons, matured and unpaid.
Capital-stock and funded-debt subscriptions, receipts for installments on.
Claims and judgments.
Customers' deposits.
Funded debt matured, with respect to which a definite agreement as to extension has not been made.
Notes payable on demand or maturing 1 year or less from date of issue.
Open accounts.
Tax assessments, past due.

NOTE.—Interest payable on notes or other evidences of indebtedness maturing serially shall be charged to account 335 if any portion of the obligation matures more than 1 year from date of issue.

338. **Amortization of discount on long-term debt.**—This account shall include during each month such proportion of the unamortized debit balance in each particular discount, premium, and debt expense account for actually outstanding long-term debt as is applicable to that period. This proportion shall be determined in accordance with instruction 15.

339. **Release of premium on long-term debt—Cr.**—This account shall include during each month such proportion of the unextinguished credit balance in each particular discount, premium, and debt expense account for actually outstanding long-term debt as is applicable to that period. This proportion shall be determined in accordance with instruction 15.

340. **Other fixed charges.**—This account shall include all items of fixed charges not provided for elsewhere properly chargeable to income of the accounting period, such as taxes paid by the company under tax-free covenants on indebtedness.

V. CONTINGENT INTEREST

341. **Contingent interest on funded debt.**—This account shall include accrued interest payable on funded debt, when a claim against income after fixed charges and prior to the interests of stockholders in the earnings of the company, such as interest on income bonds.

VI. Disposition of Net Income

342. **Contractual reservations of income.**—This account shall include reservations chargeable to income, when specifically required under the terms of mortgages, deeds of trust, orders of courts, contracts, or other agreements. (Note also instruction 31.)

Note A.—Reservations of income resting in the discretion of the company (i. e., not required by mortgages, contracts, etc.) shall be charged to account 343.

Note B.—Amounts charged to this account shall be concurrently credited to the appropriate reserve accounts.

343. **Miscellaneous reservations of income.**—This account shall include reservations of income for purposes not provided for elsewhere and not specifically required under terms of mortgages, contracts, etc. It shall include appropriations for investment in telephone plant, and income reserved at the company's discretion on account of rate litigations, etc. (Note also instruction 31.)

Note.—Amounts charged to this account shall be concurrently credited to the appropriate reserve accounts.

344. **Dividend appropriations of income.**—(A) This account shall include dividends on capital stock actually outstanding, if chargeable to income.

(B) If a dividend is not payable in cash, the consideration shall be described in the entry with sufficient particularity to identify it.

(C) This account shall be kept so that the dividends on each class of capital stock may be shown separately in the annual reports to this Commission.

Note A.—These accounts shall not include charges for dividends on capital stock issued or assumed by the company and held by or for it, whether pledged as collateral, or held in its treasury, in special deposits, or in sinking or other funds.

Note B.—Dividend appropriations of surplus shall be charged to account 416.

SURPLUS STATEMENT

CREDITS:

181. Unappropriated surplus (at beginning of period).[1]
400. Income balance.[2]
401. Credits for telephone plant sold.
402. Miscellaneous credits to surplus.

DEBITS:

410. Debits for telephone plant sold.
413. Miscellaneous debits to surplus.
414. Contractual reservations of surplus.
415. Miscellaneous reservations of surplus.
416. Dividend appropriations of surplus.
181. Unappropriated surplus (at end of period).[1]

SURPLUS ACCOUNTS

(Note particularly instruction 40)

400. **Income balance.**—An account, under this title, shall be maintained in the general books of the company. The balance of all income primary accounts (300 to 344, inclusive) shall be closed into this account at the end of each calendar year.

401. **Credits for telephone plant sold.**—This account shall include amounts creditable to surplus in accordance with instructions 25–C and 25–F, in connection with the sale of telephone plant.

402. **Miscellaneous credits to surplus.**—This account shall include amounts creditable to surplus not provided for elsewhere. Among the items which shall be credited to this account are (note instruction 8):

Amount of the credit balance in the discount, premium, and debt expense account relating to long-term debt reacquired at the time of its reacquirement. (Note instruction 15.)

Amount of the credit balance in the discount and premium account relating to capital stock reacquired at the time of its reacquirement. (Note instruction 14.)

Amounts received for abrogation of contracts.

Credits for amounts previously written off through charges to surplus.

Credits resulting from adjustments required to bring to par securities issued or assumed by the company and reacquired at a cost less than the par value. (Note also instruction 18.)

Delayed credits to income, operating revenue, and operating expense accounts as provided in instruction 5.

Forfeitures of amounts deposited under options for the sale or lease of property.

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[1] If a deficit, the balance shall be shown in red.
[2] If a loss, the balance shall be shown in red.

Profit derived from the sale of securities of other companies.
Profit derived from the sale of property carried in account 103. (Note also account 174.)
Profit derived from the sale of unexpired leases.
Unclaimed customers' deposits.
Unclaimed dividends.
Unclaimed wages and vouchered accounts written off.

NOTE.—An analysis of this account will be required in the annual reports of the company to this Commission.

410. **Debits for telephone plant sold.**—This account shall include amounts chargeable to surplus in accordance with instructions 25–C and 25–F, in connection with the sale of telephone plant.

413. **Miscellaneous debits to surplus.**—This account shall include amounts chargeable to surplus not provided for elsewhere. Among the items which shall be charged to this account are (note instruction 8):

Amortization, at the company's option, of the balance in account 201.
Amortization unprovided for elsewhere.
Amounts charged to surplus to cover past accrued depreciation not provided for. (Note also account 171.)
Amount of the debit balance in the discount, premium, and debt expense account relating to long-term debt reacquired at the time of its reacquirement. (Note instruction 15.)
Amount of the debit balances in the discount and premium, and stock expense accounts relating to capital stock reacquired at the time of its reacquirement. (Note instruction 14, also account 134.2.)
Amounts charged to surplus to extinguish all or any part of the debit balance in any particular discount, premium, and debt expense account for long-term debt actually outstanding. (Note instruction 15.)
Amounts paid for abrogation of contracts.
Appropriations to nonpar stock account. (Note instruction 16.1.)
Debits resulting from adjustments required to bring to par securities issued or assumed by the company and reacquired at a cost exceeding the par value. (Note also instruction 13.)
Delayed debits to income, operating revenue, and operating expense accounts as provided in instruction 5.
Expenses incurred in connection with the reacquisition of capital stock and long-term debt. (Note also instruction 13–B.)
Forfeitures of amounts deposited under options for the purchase or lease of property.
Inventory, appraisal, and other costs incident to the acquisition, sale, or lease of property where the transactions are abandoned.
Losses of funds due to bank failures.
Losses resulting from the sale, destruction, or retirement of property carried in account 103. (Note also account 174.)
Losses resulting from the sale of securities of other companies.
Payments of amounts previously written off through credits to surplus.

NOTE.—An analysis of this account will be required in the annual reports of the company to this Commission.

414. **Contractual reservations of surplus.**—This account shall include reservations chargeable to surplus when specifically required under the terms of mortgages, deeds of trust, orders of courts, contracts, or other agreements. (Note also instruction 31.)

NOTE A.—Reservations of surplus resting in the discretion of the company (i. e., not required by mortgages, contracts, etc.) shall be charged to account 415.

NOTE B.—Amounts charged to this account shall be concurrently credited to the appropriate reserve accounts.

415. **Miscellaneous reservations of surplus.**—This account shall include reservations of surplus for purposes not provided for elsewhere and not specifically required under terms of mortgages, contracts, etc. It shall include appropriations for investment in telephone plant and surplus reserved at the company's discretion on account of rate litigations, etc. (Note also instruction 31.)

NOTE.—Amounts charged to this account shall be concurrently credited to the appropriate reserve accounts.

416. **Dividend appropriations of surplus.**—(A) This account shall include dividends on capital stock actually outstanding, if chargeable to surplus.

(B) If a dividend is not payable in cash the consideration shall be described in the entry with sufficient particularity to identify it.

(C) This account shall be kept so that the dividends on each class of capital stock may be shown separately in the annual reports to this Commission.

NOTE A.—These accounts shall not include charges for dividends on capital stock issued or assumed by the company and held by or for it, whether pledged as collateral, or held in its treasury, in special deposits, or in sinking or other funds.

NOTE B.—Dividend appropriations of income shall be charged to account 344.

OPERATING REVENUE ACCOUNTS

Accounts for Class A Companies	Accounts for Class B Companies
I. Local Service Revenues.	I. Local Service Revenues.
500. Subscribers' station revenues.	500. Local service revenues.
501. Public telephone revenues.	
503. Service stations.	
504. Local private line services.	
506. Other local service revenues.	
II. Toll Service Revenues.	II. Toll Service Revenues.
510. Message tolls.	510. Toll service revenues.
512. Toll private line services.	
516. Other toll service revenues.	
III. Miscellaneous Revenues.	III. Miscellaneous Revenues.
521. Telegraph commissions.	520. Miscellaneous operating revenues.
523. Directory advertising and sales.	
524. Rent revenues.	
525. Revenues from general services and licenses.	
526. Other operating revenues.	
IV. Uncollectible Revenues.	IV. Uncollectible Revenues.
530. Uncollectible operating revenues—Dr.	530. Uncollectible operating revenues—Dr.

OPERATING REVENUE ACCOUNTS

(Note particularly instructions 4, 5, 6, 50, 51, and 52)

I. Local Service Revenues

500. Subscribers' station revenues.—This account shall include local service revenues from business and residence subscribers' service and from semipublic service, including such revenues from main stations, private branch exchange systems, order turrets, and other subscribers' stations, whether the charge is based upon a flat rate or a measured rate. It shall include local service revenues from mileage charges and auxiliary equipment in connection with such subscribers' service. This account shall include also revenues from directory listings for such subscribers' service

requirements, such as listings of extra names and alternate call numbers in the alphabetical sections of directories.

NOTE A.—Local service revenues from public telephones and from service stations shall be credited to accounts 501 and 503, respectively.

NOTE B.—Revenues from advertising in directories (i. e., other than listings for service requirements) shall be credited to account 523.

501. **Public telephone revenues.**—This account shall include local service revenues from public telephone service.

NOTE A.—Local service revenues from semipublic service shall be credited to account 500.

NOTE B.—Public telephone commissions shall be charged to account 648.

503. **Service stations.**—This account shall include local service revenues from stations the lines or equipment of which are provided wholly or in part by others and to which the company furnishes local service, switching service, or both.

504. **Local private line services.**—This account shall include local service revenues from private line services and facilities furnished between points in the same local service area under contracts providing exclusive service, either continuously or during stated periods (i. e., service not requiring central office switching operations). It shall include local private line service revenues from lines furnished for such purposes as telephone, telegraph, teletypewriter, public address, radio program transmission, and remote control. It shall include also charges for toll terminals and local loops furnished either continuously or during stated periods in connection with toll services (including those furnished for use in connection with lines of other companies); and charges for instruments and equipment, when furnished in connection with such lines and loops.

506. **Other local service revenues.**—This account shall include all local service revenues not provided for elsewhere.

II. TOLL SERVICE REVENUES

510. **Message tolls.**—(A) This account shall include toll service revenues from the transmission of messages, including such revenues from messages transmitted entirely over the company's own lines, and amounts representing divisions of toll service revenues received, (*a*) from messages transmitted partly over the company's lines and partly over lines of other companies, (*b*) as compensation for originating or terminating toll messages of other companies, and (*c*) as compensation for switching toll messages between lines of other companies.

(B) This account shall include revenues from guarantees at toll stations and from messenger service in notifying persons of toll calls.

512. **Toll private line services.**—This account shall include toll service revenues from private line services and facilities furnished between different local service areas under contracts providing exclusive service either continuously or during stated periods, including, (*a*) revenues from services involving only the use of the company's own lines, and (*b*) amounts representing divisions of toll private line service revenues when such service involves the use of lines of other companies. It shall include toll private line service revenues from lines furnished for such purposes as telephone, telegraph, teletypewriter, public address, radio program transmission, and remote control.

NOTE A.—Charges for local loops furnished either continuously or during stated periods and the instruments used in connection therewith (including those furnished for use in connection with lines of other companies) shall be credited to account 504.

NOTE B.—Toll service revenues from the transmission of messages charged for on a per-message basis shall be included in account 510.

516. **Other toll service revenues.**—This account shall include all toll service revenues not provided for elsewhere.

III. MISCELLANEOUS REVENUES

521. **Telegraph commissions.**—This account shall include commissions receivable for the billing or collection of telegraph, cable, or wireless tolls on messages transmitted by others.

523. **Directory advertising and sales.**—This account shall include revenues from advertising in directories and from the sale or furnishing of new directories either of the company's own issue or directories purchased from others. It shall include all revenues from the classified sections and from bold-face listings, marginal displays, inserts, cover and other advertisements in alphabetical sections of directories.

NOTE A.—Revenues from directory listings for service requirements, such as listings of extra names and alternate call numbers in the alphabetical sections of directories, shall be credited to account 500.

NOTE B.—Revenues from advertising other than in directories shall be credited to account 526.

NOTE C.—Amounts received as salvage on old directories shall be credited to account 649.

524. **Rent revenues.**—This account shall include revenues (including taxes when borne by the lessee) from the rental or subrental to others of telephone plant constituting a part of the property used by the company in its telephone operations, such as instruments, equipment, and lines furnished apart from telephone service (note instruction 3-AA) rendered by the company; space in conduits; pole line space for attachments; space in

buildings; and carrying charges on property used in joint operations. (Note also instruction 62 and note B to this account.)

NOTE A.—The expenses of maintaining and operating the rented property, including depreciation and insurance, shall be included in the appropriate operating expense accounts. Taxes applicable to the rented property shall be included by the owner of the rented property in account 305.

NOTE B.—Rents from the exclusive use of telephone operating property held as a whole and operated by others, such as a complete telephone plant, a complete exchange, or a complete toll system, shall be included in account 302.

525. **Revenues from general services and licenses.**—This account shall include amounts accruing for services rendered other companies under a license agreement, general service contract, or other arrangement providing for the furnishing of general accounting, engineering, financial, legal, patent, and other general services.

526. **Other operating revenues.**—This account shall include all miscellaneous operating revenues not provided for elsewhere, such as amounts charged for private branch exchange operating services performed by operators regularly employed by the telephone company; flat amounts (not divisions of revenue or reimbursements of costs) charged other telephone companies for operating services on toll lines of such companies terminating in the switchboard of the accounting company; revenues from advertising other than in directories; unclaimed refunds or overcharges on telephone service; and profits realized from custom work performed for others incident to the company's telephone operations.

IV. UNCOLLECTIBLE REVENUES

530. **Uncollectible operating revenues—Dr.**—(A) This account shall include amounts credited to the operating revenue accounts which have proved impracticable of collection. (Note also instruction 11 and account 118-B.)

(B) This account may include monthly charges based on estimates, to provide a reserve for uncollectible accounts due from customers and agents. Amounts thus charged to this account shall be credited to subaccount (B), "Reserve for uncollectible accounts—Cr.", under account 118, "Due from customers and agents."

(C) When revenue which has been written off through this account is collected, the amount of the collection shall be credited to this account.

NOTE.—Uncollectible amounts which have not been treated as operating revenues shall be charged to account 323, account 413, or other appropriate account.

OPERATING EXPENSE ACCOUNTS

ACCOUNTS FOR CLASS A COMPANIES.

I. MAINTENANCE EXPENSES.

602.1. Repairs of pole lines.
602.2. Repairs of aerial cable.
602.3. Repairs of underground cable.
602.4. Repairs of buried cable.
602.5. Repairs of submarine cable.
602.6. Repairs of aerial wire.
602.7. Repairs of underground conduit.
602.8. Shop repairs and salvage adjustments.
602.9. General supervision, engineering, and tool expenses.
603. Test desk work.
604. Repairs of central office equipment.
605. Repairs of station equipment.
606. Repairs of buildings and grounds.
607. Station removals and changes.
610. Maintaining transmission power.
611. Employment stabilization.
612. Other maintenance expenses.

II. DEPRECIATION AND AMORTIZATION EXPENSES.

608. Depreciation.
609. Extraordinary retirements.
613. Amortization of intangible property.

III. TRAFFIC EXPENSES.

621. General traffic supervision.
622. Service inspection and customer instruction.
624. Operators' wages.
626. Rest and lunch rooms.
627. Operators' employment and training.

ACCOUNTS FOR CLASS B COMPANIES

I. MAINTENANCE EXPENSES.

602. Repairs of outside plant.
603. Test desk work.
604. Repairs of central office equipment.
605. Repairs of station equipment.
606. Repairs of buildings and grounds.
607. Station removals and changes.
610. Maintaining transmission power.
611. Employment stabilization.
612. Other maintenance expenses.

II. DEPRECIATION AND AMORTIZATION EXPENSES.

608. Depreciation.
609. Extraordinary retirements.
613. Amortization of intangible property.

III. TRAFFIC EXPENSES.

624. Operators' wages.

629. Central office stationery and printing.	
630. Central office house service.	
631. Miscellaneous central office expenses.	
632. Public telephone expenses.	
633. Other traffic expenses.	633. Other traffic expenses.
634. Joint traffic expenses—Dr.	
635. Joint traffic expenses—Cr.	
IV. Commercial Expenses.	IV. Commercial Expenses.
640. General commercial administration.	640. Commercial expenses.
642. Advertising.	
643. Sales expense.	
644. Connecting company relations.	
645. Local commercial operations.	
648. Public telephone commissions.	
649. Directory expenses.	
650. Other commercial expenses.	
V. General Office Salaries and Expenses.	V. General Office Salaries and Expenses.
661. Executive department.	
662. Accounting department.	
663. Treasury department.	
664. Law department.	
665. Other general office salaries and expenses.	665. General office salaries and expenses.
VI. Other Operating Expenses.	VI. Other Operating Expenses.
668. Insurance.	
669. Accidents and damages.	
671. Operating rents.	
672. Relief and pensions.	
673. Telephone franchise requirements.	
674. General services and licenses.	
675. Other expenses.	675. Other operating expenses.
676. Telephone franchise requirements—Cr.	
677. Expenses charged construction—Cr.	

OPERATING EXPENSE ACCOUNTS

(Note particularly instructions 4, 5, 6, 25, and 60 to 64, inclusive)

I. Maintenance Expenses

602.1. **Repairs of pole lines.**—This account shall include the cost of repairing pole lines and the cost of maintaining right of way therefor.

Items

[Note instruction 8]

Inspecting, testing, and reporting on the condition of pole lines to determine the need for repairs or replacements.
Moving poles in connection with road and street changes. (Note also instruction 25.)
Painting and treating poles and pole butts subsequent to their installation.
Permits and privileges for maintenance work.
Replacing minor items of pole lines, including labor and material used and the removal and recovery of the items retired less salvage recovered, except when such items are replaced through the replacement of units of property. (Note also instruction 25.)
Respacing poles and crossarms.
Restoring condition of pole lines damaged by storms, fires, or other casualties. (Note also instruction 25.)
Right of way adjustments, cost of, when no additional rights are acquired.
Straightening poles and crossarms.
Tightening guys and raking guy stubs.
Transferring crossarms and guys in connection with replacements of poles and crossarms.
Trenching poles.
Trimming trees, cutting underbrush, and other work to maintain previous clearance of right of way.
Work on the property of others in connection with the maintenance of the pole lines of the company. (See also note A to this account.)

Note A.—Expenses on account of property of others damaged in connection with maintenance work (except for the cost of incidentally repairing the property of others in the course of such work) shall be charged to account 669.

Note B.—The cost of shop repairs and salvage adjustments, general supervision, engineering, and tool expenses, applicable to pole lines, shall be charged to accounts 602.8 or 602.9, as appropriate.

602.2. **Repairs of aerial cable.**—This account shall include the cost of repairing the aerial cable plant.

Items

[Note instruction 8]

Clearing defective cable pairs.
Inspecting, testing, and reporting on the condition of aerial cable plant to determine the need for repairs or replacements. (Note also account 603.)

Installing, transferring, replacing, and removing cross-connection wires and fuses in cable terminals or boxes. (See also note A to this account.)

Moving aerial cable in connection with road and street changes.

Opening, testing, splicing, and other work of transferring pairs in cable and transferring cable from one cable or stub to another cable or stub.

Permits and privileges for maintenance work.

Replacing minor items of aerial cable plant, including labor and material used and the removal and recovery of the items retired less salvage recovered, except when such items are replaced through the replacement of units of property. (Note also instruction 25.)

Restoring condition of aerial cable plant damaged by storms, fires, or other casualties. (Note also instruction 25.)

Testing for, locating, and clearing trouble. (Note also account 603.)

Tightening suspension strand and cutting out cable slack.

Transferring cable, cable boxes, and other aerial cable plant in connection with replacements of poles and crossarms.

Trimming trees, cutting underbrush, and other work to maintain previous clearances.

Work on the property of others in connection with the maintenance of the aerial cable plant of the company. (See also note B to this account.)

NOTE A.—The cost of cross-connection wires and fuses installed in the first equipment for service of cable terminals or boxes for aerial cable shall be charged to account 242.1.

NOTE B.—Expenses on account of property of others damaged in connection with maintenance work (except for the cost of incidentally repairing the property of others in the course of such work) shall be charged to account 669.

NOTE C.—The cost of shop repairs and salvage adjustments, general supervision, engineering, and tool expenses, applicable to aerial cable plant, shall be charged to accounts 602.8 or 602.9, as appropriate.

602.3. **Repairs of underground cable.**—This account shall include the cost of repairing the underground cable plant.

ITEMS

[Note instruction 8]

Clearing defective cable pairs.

Inspecting, testing, and reporting on the condition of the underground cable plant to determine the need for repairs or replacements. (Note also account 603.)

Installing, transferring, replacing, and removing cross-connection wires and fuses in cable terminals or boxes. (See also note A to this account.)

Moving underground cable in connection with road and street changes. (Note also instruction 25.)

Opening pavement and repaving in connection with repairs of underground cable.

Opening, testing, splicing, and other work of transferring pairs in cable and transferring cable from one cable or stub to another cable or stub.

Permits and privileges for maintenance work.

Replacing minor items of underground cable plant, including labor and material used and the removal and recovery of the items retired less salvage recovered, except when such items are replaced through the replacement of units of property. (Note also instruction 25.)

Reracking cables.

Restoring condition of underground cable plant damaged by storms, fires, or other casualties. (Note also instruction 25.)

Testing for, locating, and clearing trouble. (Note also account 603.)

Tests and surveys of existing plant to detect presence of electrolysis. (See note A to this account, also account 603.)

Work on the property of others in connection with the maintenance of the underground cable plant of the company. (See also note B to this account.)

NOTE A.—The cost of cross-connection wires and fuses installed in the first equipment for service of cable terminals or boxes, and the cost of tests for electrolysis made in connection with construction of underground cable shall be charged to account 242.2.

NOTE B.—Expenses on account of property of others damaged in connection with maintenance work (except for the cost of incidentally repairing the property of others in the course of such work) shall be charged to account 669.

NOTE C.—The cost of shop repairs and salvage adjustments, general supervision, engineering, and tool expenses, applicable to underground cable plant, shall be charged to accounts 602.8 or 602.9, as appropriate.

602.4. **Repairs of buried cable.**—This account shall include the cost of repairing the buried cable plant and the cost of maintaining right of way therefor.

ITEMS

[Note instruction 8]

Clearing defective cable pairs.

Inspecting, testing, and reporting on the condition of the buried cable plant to determine the need for repairs or replacements. (Note also account 603.)

Installing, transferring, replacing, and removing cross-connection wires and fuses in cable terminals or boxes. (See also note A to this account.)

Moving buried cable in connection with road and street changes. (Note also instruction 25.)

Opening, testing, splicing, and other work of transferring pairs in cable and transferring cable from one cable or stub to another cable or stub.

Permits and privileges for maintenance work.

Replacing minor items of buried cable plant, including labor and material used and the removal and recovery of the items retired less salvage recovered, except when such items are replaced through the replacement of units of property. (Note also instruction 25.)

Restoring condition of buried cable plant damaged by storms, fires, or other casualties. (Note also instruction 25.)

Right of way adjustments, cost of, when no additional rights are acquired.

Testing for, locating, and clearing trouble. (Note also account 603.)

Work on the property of others in connection with the maintenance of the buried cable plant of the company. (See also note B to this account.)

NOTE A.—The cost of cross-connection wires and fuses installed in the first equipment for service of cable terminals or boxes for buried cable shall be charged to account 242.3.

NOTE B.—Expenses on account of property of others damaged in connection with maintenance work (except for the cost of incidentally repairing the property of others in the course of such work) shall be charged to account 669.

NOTE C.—The cost of shop repairs and salvage adjustments, general supervision, engineering, and tool expenses, applicable to buried cable plant, shall be charged to accounts 602.8 or 602.9, as appropriate.

602.5. **Repairs of submarine cable.**—This account shall include the cost of repairing the submarine cable plant and the cost of maintaining right of way therefor.

ITEMS

[Note instruction 8]

Clearing defective cable pairs.

Inspecting, testing, and reporting on the condition of submarine cable plant to determine the need for repairs or replacements. (Note also account 603.)

Installing, transferring, replacing, and removing cross-connection wires and fuses in cable terminals or boxes. (See also note A to this account.)

Opening, testing, splicing, and other work of transferring pairs in cable and transferring cable from one cable or stub to another cable or stub.

Permits and privileges for maintenance work.

Replacing minor items of submarine cable plant, including labor and material used and the removal and recovery of the items retired less salvage recovered, except when such items are replaced through the replacement of units of property. (Note also instruction 25.)

Restoring condition of submarine cable plant damaged by storms, fires, or other casualties. (Note also instruction 25.)

Right of way adjustments, cost of, when no additional rights are acquired.

Testing for, locating, and clearing trouble. (Note also account 603.)

Work on the property of others in connection with the maintenance of the submarine cable plant of the company. (See also note B to this account.)

NOTE A.—The cost of cross-connection wires and fuses installed in the first equipment for service of cable terminals or boxes for submarine cable shall be charged to account 242.4.

NOTE B.—Expenses on account of property of others damaged in connection with maintenance work (except for the cost of incidentally repairing property of others in the course of such work) shall be charged to account 669.

NOTE C.—The cost of shop repairs and salvage adjustments, general supervision, engineering, and tool expenses, applicable to submarine cable plant, shall be charged to accounts 602.8 or 602.9, as appropriate.

602.6. **Repairs of aerial wire.**—This account shall include the cost of repairing the aerial wire plant.

ITEMS

[Note instruction 8]

Cutting out or cutting in slack in aerial wire.
Inspecting, testing, and reporting on the condition of aerial wire plant to determine the need for repairs or replacements. (Note also account 603.)
Moving aerial wire in connection with road and street changes. (Note also instruction 25.)
Permits and privileges for maintenance work.
Rearranging wires on pins.
Replacing minor items of aerial wire plant, including labor and material used and the removal and recovery of the items retired less salvage recovered, except when such items are replaced through the replacement of units of property. (Note also instruction 25.)
Restoring condition of aerial wire plant damaged by storms, fires, or other casualties. (Note also instruction 25.)
Testing for, locating, and clearing trouble. (Note also account 603.)
Transferring aerial wire in connection with replacements of poles and crossarms.
Transposing or retransposing existing aerial wire, including such work for the removal of electric interference and for the creation of phantom and carrier circuits subsequent to the original installation of the wires. (See also note A to this account.)
Trimming trees, cutting underbrush, and other work to maintain previous clearances.
Work on the property of others in connection with the maintenance of the aerial wire plant of the company. (See also note B to this account.)

NOTE A.—The cost of any betterments and plant added resulting from such work shall be included in account 243.

NOTE B.—Expenses on account of property of others damaged in connection with maintenance work (except for the cost of incidentally repairing the property of others in the course of such work) shall be charged to account 669.

NOTE C.—The cost of shop repairs and salvage adjustments, general supervision, engineering, and tool expenses, applicable to aerial wire plant, shall be charged to accounts 602.8 or 602.9, as appropriate.

602.7. **Repairs of underground conduit.**—This account shall include the cost of repairing the underground conduit plant and the cost of maintaining right of way therefor.

ITEMS

[Note instruction 8]

Cleaning manholes and ducts. (See also note A to this account.)
Moving underground conduit in connection with road and street changes. (Note also instruction 25.)
Opening pavement and repaving in connection with repairs of underground conduit plant.
Permits and privileges for maintenance work.

Replacing minor items of underground conduit plant, including labor and material used and the removal and recovery of the items retired less salvage recovered, except when such items are replaced through the replacement of units of property. (Note also instruction 25.)

Restoring condition of underground conduit plant damaged by storms, fires, or other casualties. (Note also instruction 25.)

Right of way adjustments, cost of, when no additional rights are acquired.

Work on the property of others in connection with the maintenance of the underground conduit plant of the company. (See also note B to this account.)

NOTE A.—The cost of cleaning manholes and ducts in connection with construction work and not necessary in the maintenance or operation of the plant shall be included in the account chargeable with the cost of the construction work.

NOTE B.—Expenses on account of property of others damaged in connection with maintenance work (except for the cost of incidentally repairing property of others in the course of such work) shall be charged to account 669.

NOTE C.—The cost of shop repairs and salvage adjustments, general supervision, engineering, and tool expenses, applicable to underground conduit, shall be charged to accounts 602.8 or 602.9, as appropriate.

602.8. **Shop repairs and salvage adjustments.**—This account shall include the cost of repairs and conversions of pole line, cable, aerial wire, and underground conduit material which has been removed from plant and returned to shops for repairs. It shall also include salvage adjustments with respect to such material which cannot be practicably allocated to accounts 602.1 to 602.7, inclusive.

602.9. **General supervision, engineering, and tool expenses.**—This account shall include the cost of engineering and plant supervision expense applicable to work charged to accounts 602.1 to 602.8, inclusive. It shall also include amounts cleared from account 702, "Vehicle and other work equipment expense", for expense of small tools applicable to repairs of outside plant.

603. **Test desk work.**—(A) This account shall include the costs incurred, in connection with maintenance of outside plant, by forces located in central offices and engaged in the work of receiving and recording reports of trouble from subscribers and others; testing from test desks to determine the nature and location of trouble; dispatching repairmen from test desks; testing from test desks with repairmen during the course of their work or upon its completion and making other tests from test desks to determine the condition of the plant; and testing from test desks in the course of station reconnections, reinstallations, inside moves and rearrangements of station equipment.

(B) This account shall include also the cost of cable fault location work performed at specially equipped test desks; the cost of putting up and taking down leased toll circuits; monitoring, test-

ing and adjusting leased toll circuits to maintain such circuits in proper adjustment; and similar work in connection with toll message circuits.

604. **Repairs of central office equipment.**—(A) This account shall include the cost of repairing central office equipment.

(B) This account shall include also the pay and expenses of plant department forces engaged in maintaining and operating equipment for producing electricity for transmitting traffic and operating signals.

ITEMS

[Note instruction 8]

Adding acid and water to batteries and reading specific gravity, current drain, and voltage of batteries.
Cleaning equipment.
Disconnecting and reconnecting customers' lines in central offices for temporary periods of nonuse or for nonpayment of bills.
Disconnecting customers' lines in central offices due to termination of service.
House service. (Note also account 707.)
Lubrication, adjustment, and cleaning of power equipment, including the lubrication and cleaning of drive motors and driving mechanism in panel offices.
Operating prime movers, generators, and motors.
Rearranging and replacing frame cross-connection wires. (See also note A to this account.)
Regulating power for repeaters.
Removing sediment from storage batteries and the cost of repairing storage batteries, including replacement of minor items.
Repairing used central office equipment for reuse.
Replacement of central office dry cell batteries.
Replacing minor items of central office equipment, including labor and material used and the removal and recovery of the items retired less salvage recovered, except when such items are replaced through the replacement of units of property. (Note also instruction 25.)
Starting, stopping, and watching operation of power equipment.
Supplies, such as acid, caustic soda, cheesecloth, commutator paste, dry cells, electrolyte, kerosene, oil and waste.
Testing for, locating, and clearing trouble. (See also note B to this account.)
Tools and other individual central office equipment—items of small value or short life, cost and repairs of. (Note also instruction 20–D.)
Training employees for central office repair work.
Underlining switchboard jacks, renewing switchboard markings, and placing and changing number plates and designation strips, not incident to construction. (See also note C to this account.)
Watching and regulating the operation of repeaters, duplex and multiplex apparatus on telephone and telegraph lines.

NOTE A.—The cost of work on central office frames incident to routine station and line turnover and growth, including the placing, removing, or rearrangement of cross-connections (including the cost, less salvage, of the cross-connection wire, heat coils, protector blocks, etc.), and the opening and closing of lines on the frame, may be currently charged direct to this account and, before the close of the calendar year, adjust-

ment made between this account and account 221 for the net increase in central office investment or between account 221 and account 171 for the net decrease in such investment, due to increase or decrease in lines.

NOTE B.—The pay and expenses of test-board men and other employees in central offices engaged in testing circuits in connection with the maintenance of plant outside of central offices, such as testing with station repairmen, cablemen, etc., shall be charged to account 603. Similar costs in connection with construction projects shall be included in the telephone plant accounts appropriate for the class of plant tested.

NOTE C.—The pay of clerks of the traffic department when engaged in such work shall be charged to account 624. The cost of placing number plates, designation strips, making switchboard markings, and similar work in connection with central office construction shall be included in account 221. (Note also instruction 63.)

NOTE D.—The cost of power produced for house service purposes shall be charged to account 707 or other account, as may be appropriate.

NOTE E.—The cost of electricity purchased and the cost of coal, gas, gasoline, oil, and other fuel used in the generation, conversion, and storage of current for transmitting traffic and operating signals shall be included in account 610.

605. **Repairs of station equipment.**—(A) This account shall include the cost of repairing station apparatus, station installations (including inside wires), drop and block wires, private branch exchanges and booths, and special fittings.

(B) This account shall include also such costs of extensive replacements of station apparatus and inside, drop and block wires, which, under conditions provided in instruction 64, have been carried in account 138, "Extraordinary maintenance and retirements."

ITEMS

[Note instruction 8]

Changing type of station apparatus, such as from desk set to hand set, wall set to desk set, magneto to common battery, or nondial to dial. (See also note A to this account.)

Changing drop wires from street to alley or interior block distribution, *together with associated* changes of inside wires.

Cleaning equipment.

Inside moves (moves or relocations on the same premises or at the same address) of station apparatus, private branch exchanges and booths, and special fittings. (See also note B to this account.)

Inspecting, testing, and reporting on condition of equipment to determine the need for repairs or [illegible]lacements. (Note also account 603.)

Labor, traveling, and other incidental costs of replacing any items (including "units of property") of station apparatus. (See also note A to this account.)

Material used in replacing minor items of station apparatus. (Note also instruction 25.)

Number plate changes not incident to station reconnections.

Relocating inside, drop, and block wires.

Removing sediment from and cleaning private branch exchange batteries.

Repainting and other repairs of booths, including those owned by others.

Repairing used station equipment for reuse.

Repairing furniture and equipment classified in account 235, and cost and repairs of individual items of small value or short life. (Note also instruction 20–D.)

Replacing minor items of private branch exchanges and booths and special fittings, including labor and material used and the removal and recovery of the items retired less salvage recovered, except when such items are replaced through the replacement of units of property. (Note also instruction 25.)

Replacing inside, drop, and block wires.

Replacing station batteries.

Retirement (original cost, plus cost of removal less salvage recovered) of drop or block wires, in the course of extensive plant rearrangements, such as the replacement of such wires by cable.

Routine work to prevent trouble, such as trimming trees to protect existing drop wires.

Testing for, locating, and clearing trouble in station equipment. (Note also account 603.)

NOTE A.—The cost of plant added (such as dials) or betterments of station apparatus shall be charged to account 231. When a "unit of property" (note also instructions 24 and 25) of station apparatus is replaced, account 231 shall be charged with the cost of the material installed and credited with the cost of the material retired; the latter amount less the value of salvage recovered shall be charged to account 171.

NOTE B.—Moves of stations, private branch exchanges and booths, and special fittings to different premises or to a different address shall be accounted for as removals or disconnections, as appropriate, from the old location, and as new installations, reinstallations, or reconnections, as appropriate, at the new location. (Note also account 607.)

NOTE C.—Amounts charged customers for moves and changes of station equipment shall be credited to account 500 or to other revenue accounts appropriate for the class of service involved.

606. **Repairs of buildings and grounds.**—This account shall include the cost of repairing buildings and grounds, their fixtures and appurtenances, except as provided in the texts of the clearing accounts with respect to rented quarters.

ITEMS

[Note instruction 8]

Changing location of partitions. (See also note A to this account.)

Maintaining public improvements, including assessments covering such work.

Maintaining yards and grounds, including their fences, shrubbery, sidewalks, and sewers.

Minor improvements to leased buildings, quarters, and grounds. (Note also instruction 23.)

Repainting and repapering buildings, including redecorating interiors of buildings.

Repairing building machinery, fixtures, appurtenances, and appliances, such as elevators, plumbing, and equipment for heating, lighting, and ventilating.

Repairing rented buildings, quarters, and grounds, except when the rented property is used in operations the expense of which is chargeable to the clearing accounts.

Replacing and repairing awnings, screens, window shades and ventilators, storm doors, storm windows, movable partitions, and similar movable minor items of buildings. (See also note B to this account.)

Replacing minor items of buildings, including labor and material used and the removal and recovery of the items retired less salvage recovered, except when such items are replaced through the replacement of units of property. (See also instruction 25 and note C to this account.)

Restoring condition of buildings or grounds damaged in the course of repairs, replacements, additions, or betterments. (See also note C to this account.)

NOTE A.—The cost of any substantial increase or decrease in partitions resulting from such changes shall be charged or credited, as appropriate, to account 212.

NOTE B.—When partitions of a movable type (for example, steel and glass, or wood and glass) are replaced by partitions of a permanent type (for example, terra cotta) or vice versa, the costs involved shall be accounted for through the telephone plant and depreciation reserve accounts.

NOTE C.—The cost of minor building alterations incident to the installation of central office equipment, such as opening and closing holes in ceilings, partitions, walls, and floors to permit installation of equipment, power conduit and wiring, shall be charged to account 221.

NOTE D.—The cost of initial improvements (including repairs, rearrangements, plant added, and betterments) in the preparation for service of either rented or purchased buildings or grounds shall be charged to account 211 or account 212, as appropriate, except that when the improvements to leased property are of relatively minor cost or short life or the period of the lease is less than 1 year, the cost shall be charged to the account chargeable with the cost of repairs of such property. (Note also instruction 23.)

NOTE E.—The cost of repairs to buildings and grounds classable under account 103 shall be charged to account 315.

607. **Station removals and changes.**—(A) This account shall include the expense of removing stations due to the termination of service together with the resultant loss of investment in station installations, drop and block wires, and the expense of station disconnections, reconnections, and reinstallations, as follows:

(B) When stations are removed from subscribers' premises, the original cost (actual or estimated average unit cost) of the station installations (including inside wires) carried in account 232, "Station installations", and of any drop and block wires thereby retired from service, shall be credited to the appropriate telephone plant accounts and charged to this account, which shall be credited with the value of any salvage recovered therefrom. The cost of removing the station apparatus, inside, drop and block wires, including transportation costs incurred in the recovery of the material, shall be charged to this account.

(C) When stations are disconnected (either for nonpayment or other discontinuance of service) but left on premises, this account shall be charged with the cost of disconnecting the station equip-

ment; and when reconnected, the cost of reconnecting shall also be charged hereto.

(D) When stations are reinstalled on premises from which the station apparatus had previously been removed, if inside wire or ground wire left from a previous installation is reused, wholly or in part, the cost of installing the station apparatus (not including the cost of the apparatus which shall be charged to account 231) and of placing the inside wire again in service shall be charged to this account, and this account shall be credited and account 232, "Station installations", charged with the average cost of a station installation (including inside wire) in place; if drop or block wire left from a previous installation is reused, wholly or in part, the cost of placing such wire again in service shall be charged to this account, and this account shall be credited and account 233, "Drop and block wires", charged with the average cost of a drop or block wire in place.

NOTE A.—The cost of disconnecting and reconnecting subscribers' lines in central offices shall be charged to account 604. The cost of test desk work in connection with station removals and changes shall be charged to account 603.

NOTE B.—Amounts charged subscribers for restoration of service shall be credited to account 500 or to other revenue accounts appropriate for the class of service involved.

610. **Maintaining transmission power.**—This account shall include the cost of power for transmitting traffic and operating signals. It shall include the cost of electricity purchased and the cost of coal, gas, gasoline, oil, and other fuel used in the generation, conversion, and storage of current for operating dial system, repeater, and carrier equipment, ringing machines, ticket-distributor systems, battery-charging machines, coin-collection equipment, and for other transmission power requirements of central office equipment, private branch exchanges, and other station equipment.

NOTE A.—Payments for the installation in central offices of permanent power circuits for emergency use shall be charged to the appropriate plant account. Payments to others made with a provision for reimbursement as power is used shall be treated as a prepayment and cleared by charges to this account or other appropriate account.

NOTE B.—The cost of power produced for house service purposes shall be charged to account 707 or other account, as may be appropriate.

NOTE C.—The pay and expenses of central office forces engaged in the generation, conversion, and regulation of transmission power shall be charged to account 604.

611. **Employment stabilization.**—(A) This account shall include amounts systematically accrued with respect to maintenance work to be performed in accordance with an employment stabilization program designed to spread the total volume of maintenance work more evenly from year to year. Charges to this account shall be made only after approval by this Commission of the company's employment stabilization program, the plan of administra-

tion of the program, the character of the work to which sums accrued may subsequently be applied, and the amount of the monthly or annual accruals for stabilization purposes.

(B) Amounts charged to this account shall concurrently be credited to account 173, "Employment stabilization reserve."

(C) When maintenance work for which provision has been made through this account is performed, the cost of such work shall be charged to the appropriate maintenance expense accounts. Concurrently, this account shall be credited and account 173, "Employment stabilization reserve", shall be charged with an amount equal to the cost of such work.

612. **Other maintenance expenses.**—This account shall include all maintenance expenses not properly chargeable to other accounts.

II. Depreciation and Amortization Expenses

608. **Depreciation.**—This account shall include the amount of depreciation charges applicable to the accounting period for all classes of depreciable telephone plant, except amounts chargeable to clearing accounts. The depreciation charges shall be made in accordance with instructions 23–C, 80, 81, and 82. (Note accounts 315 and 174 for depreciation of miscellaneous physical property.)

609. **Extraordinary retirements.**—This account shall include the proportion of the service value of telephone plant retired, carried in account 138, "Extraordinary maintenance and retirements", which by specific authority of this Commission shall be charged to operating expenses for the period. (Note also instruction 83 and account 138.)

613. **Amortization of intangible property.**—This account shall be charged each month with the amount necessary to cover such portions of the lives of limited term franchises, patents, leaseholds, and similar intangible property included in the telephone plant accounts, as have expired during the month. Amounts so charged shall be credited to account 172, "Amortization reserve."

III. Traffic Expenses

621. **General traffic supervision.**—This account shall include the pay, office, traveling, and other expenses of officers directly in charge of the general supervision of traffic, either for the company as a whole or a territorial subdivision; also the pay and expenses of their assistants and office forces.

Items

[Note instruction 8]

House service. (Note also account 707.)

Medical examiners and their assistants, welfare supervisors, and nurses engaged in the traffic department, pay and expenses of. (See also note A to this account.)

Office supplies.
Postage, printing, and stationery.
Preparing tariff and route data, traffic department's expense of. (See also note B to this account.)
Repairs of furniture and office equipment, and cost and repairs of individual items of small value or short life.
Traffic superintendents, managers, chiefs, supervisors, and engineers, pay and expenses of. (See also note C to this account.)
Traveling expenses.

NOTE A.—The pay and expenses of physicians and nurses engaged in work such as conducting physical examinations of employees for all departments, giving general health advice, providing first-aid treatment, supervising and investigating sickness cases, and in other general relief activities shall be charged to account 672. The pay of nurses assigned to operators' quarters shall be charged to account 626.

NOTE B.—The traffic department's proportion of the expense of printing and distributing tariff and route data shall be charged to account 629.

NOTE C.—The cost of traffic engineering applicable to construction shall be credited to this account.

622. Service inspection and customer instruction.—(A) This account shall include the pay, office, traveling, and other expenses of service observation forces. It shall include also the expense of inspecting and directly supervising private branch exchange service.

(B) This account shall also be charged with the expense of instructing customers in methods of placing calls, including instruction in the use of dial equipment. (See also note A to this account.)

ITEMS

[Note instruction 8]

Card notices and other literature for instruction of customers in use of dial equipment.
Employment and training of private branch exchange operators apart from the regular employment and training of operators.
House service. (Note also account 707.)
Investigation and adjustment of traffic service complaints. (See also note B to this account.)
Making test calls.
Observation of handling of traffic by operators. (See also note C to this account.)
Observation of accuracy of measured service charges.
Office supplies.
Postage, printing, and stationery.
Private branch exchange service supervisors, pay and expense of.
Repairs of furniture and office equipment, and cost and repairs of individual items of small value or short life.
Stop watches, repairs of.
Summarization of service observation data.
Traveling expenses.

NOTE A.—The expense of instructing customers in the use of station equipment in the course of station installation activities shall be included in the accounts charged with the cost of such activities.

NOTE B.—The recording and adjustment of traffic service complaints performed by operating forces in the course of completing calls shall be included in account 624.

NOTE C.—The pay of operators, supervisors, and other employees in central office operating rooms engaged in listening-in work in connection with coaching operators shall be charged to account 624.

624. **Operators' wages.**—(A) This account shall include the pay of chief operators, assistant chief operators, monitors, supervisors, ticket distributors, switchboard operators, information operators, directory operators, private branch exchange operators, telegraph operators, teletypewriter operators, operators employed in quoting toll rates and charges, listening-in work in connection with coaching operators, helping subscribers to place and complete calls together with the incidental recording of subscribers' complaints, operating telephotographic equipment, and all other operators employed in the operation of central office and private branch exchange equipment.

(B) This account shall include also the pay of clerks, stenographers, and messengers engaged in line assignments, peg counts, message register readings, plug counts, preparing time or attendance records, pay rolls, intercepting records, panel and jack records, line and station reports, delivering messages or notifying persons of calls, and similar traffic work performed in central offices or centralized outside of central offices. It shall include the pay of such employees while engaged in underlining switchboard jacks and placing and changing number plates and designation strips.

NOTE A.—The pay of operators at public telephone stations shall be charged to account 632.

NOTE B.—Commissions or agency-contract allowances paid to exchange agents or managers in lieu of salary, operating expenses, etc., shall be equitably apportioned to construction, maintenance, traffic, commercial, or other accounts affected.

NOTE C.—The pay and expenses of operators, supervisors, chief operators, etc., while attending supplemental training or post-graduate operating schools shall be charged to account 627.

626. **Rest and lunch rooms.**—This account shall include the cost of operating rest and lunch rooms for central office employees, including the cost of meals provided for such employees. This includes the cost of operating such facilities as rest rooms, quiet rooms, reading rooms, medical rooms, locker rooms, check rooms, sleeping rooms, and dormitories. Credit to this account amounts received for meals served.

ITEMS

[Note instruction 8]

Bedding.
Dishes.
Electric power for cooking, refrigeration, or operating kitchen equipment.
Food supplies.
Fuel for cooking.
Handling orders and bills for supplies.
House service. (Note also account 707.)

Ice for refrigeration.
Laundry.
Linen.
Lunch-room managers, cooks, cashiers, waiters, and kitchen helpers, pay and expenses of.
Medical supplies, including first-aid materials, used in operators' quarters.
Newspapers, magazines, and phonograph records.
Nurses, matrons, and attendants for operators' quarters, pay and expenses of.
Postage, printing, and stationery.
Repairs of furniture and equipment, and cost and repairs of individual items of small value or short life.
Silverware.
Uniforms.

NOTE.—The net cost of operating central office rest and lunch rooms used, except incidentally, by other than employees of the traffic department shall be apportioned on an equitable basis to the departments benefited.

627. **Operators' employment and training.**—This account shall include expenses incurred in the employment and training of operators whether or not a school is maintained.

ITEMS

[Note instruction 8]

Advertising for operators, cost of.
Amounts paid employees for securing new operators.
Pay and expenses of employees engaged in the employment of operators and in interviewing applicants.
Pay and expenses of instructors, messengers, personnel supervisors, etc., in schools.
Pay of operators, supervisors, chief operators, etc., attending supplemental training or post-graduate courses.
Pay of student operators rendering no service.
Postage, printing, and stationery.
Repairs of furniture and office equipment, and cost and repairs of individual items of small value or short life.
Supplies for employment and school work.
Traveling expenses.

NOTE.—The cost of house service for operators' schools shall be charged to account 630. (Note also account 707.)

629. **Central office stationery and printing.**—This account shall include the cost of postage, printing, and stationery for use in central offices except as provided for elsewhere.

ITEMS

[Note instruction 8]

Office supplies.
Postage on toll tickets forwarded by connecting companies.
Postage on toll tickets from central offices to accounting offices.
Printing and distributing tariff and route data, traffic department's proportion of cost of. (See also note A to this account.)

Printing directories of telephone numbers by street addresses, traffic department's expense of. (See also note B to this account.)
Tickets and other central office stationery and supplies furnished connecting companies.
Toll tickets.

NOTE A.—The expense of preparing tariff and route data incurred by the traffic department shall be charged to account 621.

NOTE B.—The cost of such directories prepared by the directory department shall be charged to account 649.

630. **Central office house service.**—This account shall include the cost of light, heat, janitor service, and other care of central office traffic quarters except as provided in account 626, "Rest and lunch rooms." (Note also account 707.)

ITEMS

[Note instruction 8]

Electricity for elevators, fans, lights, and ventilators. (See also note A to this account.)
Fuel, ice, towels, water, toilet, and other supplies.

NOTE A.—The cost of electricity used in connection with central office equipment installations shall be charged to account 221.

NOTE B.—The cost of house service for central office plant quarters shall be charged to account 604 or to an appropriate clearing account.

631. **Miscellaneous central office expenses.**—This account shall include the cost of operating central offices not chargeable to other accounts.

ITEMS

[Note instruction 8]

Board and lodging for operators.
Clothing furnished operators in emergencies.
Films for message register readings.
Laundry of equipment used by operators.
Messenger service. (See also note A to this account.)
Paint brushes, paint, and other articles used by traffic employees in switchboard markings.
Photographic supplies for telephotographic work.
Rent of typewriters for central offices.
Repairs of furniture and office equipment, and cost and repairs of individual items of small value or short life used in central office operating quarters. (See also note B to this account.)
Time service furnished the company by others.
Transportation for divided tour operators.
Traveling expenses of employees whose pay is chargeable to account 624.

NOTE A.—The pay of company employees engaged in central office messenger service shall be charged to account 624.

NOTE B.—Repairs of furniture and office equipment and the cost and repairs of individual items of small value or short life used in central office plant quarters shall be charged to account 604 or to an appropriate clearing account. Such costs for items used in rest and lunch room quarters shall be charged to account 626, and those for items used in operators' employment and school quarters shall be charged to account 627.

632. **Public telephone expenses.**—This account shall include all traffic expenses, except central office operating expenses, incurred in connection with the operation of public telephones.

ITEMS

[Note instruction 8]

Attendants, clerks, messengers, and operators at public telephones, pay and expenses of.
Employees engaged in direct supervision of the operation of public telephone service, pay and expenses of.
House service. (Note also account 707.)
Instruction cards for booths.
Postage, printing, and stationery.
Traveling expenses.
Uniforms.

NOTE.—Commissions, percentages of receipts, and flat sums paid for occupancy privileges for public telephones shall be charged to account 648.

633. **Other traffic expenses.**—This account shall include all traffic expenses not properly chargeable to other accounts.

NOTE A.—Rent paid for central offices shall be charged to account 671.
NOTE B.—Traffic expenses incurred in the operation of special-type equipment, such as public-address systems, telephotographic, radio broadcasting and receiving, motion-picture and public-demonstration equipment, shall be charged, so far as practicable, to the traffic expense accounts provided for the expenses of regular telephone operations.

634. **Joint traffic expenses—Dr.**—This account may include amounts payable to other telephone companies for joint traffic expenses, as provided in instruction 62.

635. **Joint traffic expenses—Cr.**—This account may include amounts receivable from other telephone companies for joint traffic expenses, as provided in instruction 62.

IV. COMMERCIAL EXPENSES

640. **General commercial administration.**—This account shall include the pay, office, traveling, and other expenses of officers directly in charge of the general administration of the commercial department either for the company as a whole or a territorial subdivision; also the pay and expenses of their assistants and office forces.

ITEMS

[Note instruction 8]

Commercial surveys, forecasts, rate-plan studies, and development studies. (See also note B to this account.)
General, division, and district commercial managers, supervisors, superintendents, and engineers, pay and expenses of. (See also notes A and B to this account.)
House service. (Note also account 707.)
Office supplies.
Postage, printing, and stationery.

Preparing, printing, and distributing tariff and route data, commercial department's expense of.
Repairs of furniture and office equipment, and cost and repairs of individual items of small value or short life.
Traveling expenses.

NOTE A.—The pay and expenses of an employee engaged in direct supervision of commercial activities, the cost of which is provided for in specific accounts, such as a manager in direct charge of local commercial operations, an advertising manager, a supervisor in direct charge of a group of salesmen, a directory manager, or a representative in charge of connecting company relations, shall be charged to the account or accounts provided for such costs.

NOTE B.—The cost of commercial engineering applicable to construction shall be credited to this account.

642. **Advertising.**—This account shall include expenses incurred in commercial advertising activities, including expenses incurred in giving public demonstrations of telephones, switchboards, etc.

ITEMS

[Note instruction 8]

Announcements of rate changes. (See also note A to this account.)
Commercial advertisements in newspapers and magazines. (See also note A to this account.)
Commercial advertising matter such as posters, bulletins, booklets, and related items. (See also note A to this account.)
Electric current consumed in illuminating public telephone signs.
Exhibits in connection with industrial expositions, expenses of. (See also note B to this account.)
House service. (Note also account 707.)
Lecture and demonstration tours for promotion purposes. (See also note B to this account.)
Managers and their office forces in charge of advertising and publicity, pay and expenses of.
Motion pictures.
Office supplies.
Postage, printing, and stationery.
Promotional advertising in the company's directories, such as colored page inserts, when additional printing and binding costs are incurred.
Radio programs.
Repairs of furniture and office equipment, and cost and repairs of individual items of small value or short life.
Traveling expenses.
Window displays.

NOTE A.—The cost of newspaper advertisements, literature, etc., other than for commercial advertising purposes, such as advertisements of stock and bond issues, advertising for operators, notices of dividends declared, and advertisements for sale of directory advertising, or to popularize and increase use of classified sections of directories, shall be charged to the accounts appropriate for such costs.

NOTE B.—The pay and expenses of employees performing incidental services in connection with industrial exhibits and public demonstrations of telephones, switchboards, etc., shall be included in the accounts chargeable

with the pay and expenses of the employees' regular activities. (Note also instruction 63.)

NOTE C.—The cost of flags, bunting, and similar expenses of decorating buildings shall be charged to account 707 or to the appropriate expense account of the department concerned.

643. **Sales expense.**—This account shall include expenses incurred in canvassing for new business or for changing or renewing existing service, also in interviewing customers for promoting the further use of service.

ITEMS

[Note instruction 8]

Canvassers and salesmen, pay and expenses of. (See also note to this account.)
Canvassing for purpose of regrading service or for sale of additional service.
Commercial service studies of subscribers' service.
House service. (Note also account 707.)
Office supplies.
Postage, printing, and stationery.
Repairs of furniture and office equipment, and cost and repairs of individual items of small value or short life.
Traveling expenses.

NOTE.—The pay and expenses of employees engaged in securing advertisements for directories shall be charged to account 132 or account 649, as may be appropriate.

644. **Connecting company relations.**—This account shall include expenses incurred in developing the interchange of business and other promotion of relations with connecting companies. This includes the pay and expenses of commercial representatives and their office forces engaged in the negotiation or revision of traffic agreements, assisting connecting companies in the development of toll business and similar promotion of relations with connecting companies.

ITEMS

[Note instruction 8]

Connecting company agents or representatives and their office forces, pay and expenses of.
House service. (Note also account 707.)
Office supplies.
Postage, printing, and stationery.
Repairs of furniture and office equipment, and cost and repairs of individual items of small value or short life.
Traveling expenses.

645. **Local commercial operations.**—This account shall include the pay, office, traveling, and other expenses of employees engaged in local commercial operations other than promotion or directory. This includes employees of business and collection offices engaged in preparing, changing, and handling contract or service orders,

collecting revenue and handling miscellaneous commercial relations with customers.

ITEMS

[Note instruction 8]

Badges.
Business office signs on windows, doors, etc.
Coin-box collectors, guards and supervisors of coin-box collections, pay and expenses of.
Customers' accounts, cost of keeping and billing, when performed in the course of local commercial operations. (See also note C to this account.)
Fees paid banks or others for collection of customers' bills. (For law expenses see account 664.)
House service. (Note also account 707.)
Managers in charge of local commercial operations, supervisors, counter men, bookkeepers, cashiers, clerks, and collectors, pay and expenses of. (See also note C to this account.)
Office supplies.
Postage, printing, and stationery.
Repairs of furniture and office equipment, and cost and repairs of individual items of small value or short life.
Traveling expenses.

NOTE A.—This account shall include the entire pay and expenses of employees in business offices who are only incidentally engaged in promotion or directory work. If such employees are assigned all or a part of their time to promotion or directory work, equitable portions of their pay and expenses shall be charged to the accounts provided for such expenses. (Note also instruction 63.)

NOTE B.—The cost of duplicating, recording, and handling contract or service orders after preparation by the commercial department shall be charged to the accounts of the department incurring the expense.

NOTE C.—When customers' accounts are kept and bills rendered by the accounting department, the expense involved, including pay and expenses of bookkeepers and clerks, shall be charged to account 662.

648. **Public telephone commissions.**—This account shall include amounts paid, either in the form of percentages of receipts, flat amounts deducted from receipts or other specified sums, to the owners or tenants of premises upon which attended and nonattended public and semipublic telephone stations are located, as general compensation for occupancy privileges, light, heat, attendance, and all services rendered incident to the furnishing of service from such stations.

NOTE.—The pay of operators and other attendants employed by the company at public telephone stations shall be charged to account 632.

649. **Directory expenses.**—This account shall include expenses incurred in preparing copy, printing, binding, and distributing directories, and the cost of securing advertisements for directories. It shall include also the cost of directories of other companies purchased for the use of the company or for distribution or sale to its customers. This account shall be credited with amounts received as salvage on old directories. (Note also account 132.)

ITEMS

[Note instruction 8]

Advertisements for promotion of directory advertising.
Commissions paid employees or agents for securing directory advertisements.
Directory covers.
Directory managers, clerks, advertising salesmen, and other employees of the directory department, pay and expenses of.
House service. (Note also account 707.)
Maintaining directory delivery records.
Office supplies.
Official branch exchange directories prepared by directory department, cost of.
Postage, printing, and stationery.
Preparing and printing special editions of directories, including addenda thereto, by the directory department for use of traffic department. (See also note C to this account.)
Preparing and printing street address, toll and other special directories, including addenda thereto, by directory department. (See also note C to this account.)
Repairs of furniture and office equipment, and cost and repairs of individual items of small value or short life.
Transportation and distribution of directories, cost of.
Traveling expenses.

NOTE A.—All directory expenses may be initially charged to account 132, but shall be cleared to account 649 during the months to which such expenses apply.

NOTE B.—Receipts from the sale or furnishing of new directories, either of a company's own issue or directories purchased from others, shall be credited to account 523.

NOTE C.—When such directories are prepared and issued by the traffic department, the costs involved shall be included in the appropriate traffic expense accounts.

NOTE D.—Any additional printing and binding costs incurred on account of the company's promotional advertising in its directories, such as colored page inserts, shall be charged to account 642.

650. **Other commercial expenses.**—This account shall include all commercial expenses not properly chargeable to other accounts. It shall include any definitely known amounts of losses of revenue collections due to fire or theft, (*a*) at customers' coin-box stations, (*b*) at public or semipublic telephone stations, (*c*) in the possession of collectors en route to collection offices, (*d*) on hand at collection offices, and (*e*) between collection offices and banks.

NOTE A.—Rent paid for commercial offices shall be charged to account 671.

NOTE B.—Commercial expenses incurred in connection with public demonstrations and such services as public address and telephotograph operations shall be charged, so far as practicable, to the commercial expense accounts provided for the expenses of regular telephone operations.

V. GENERAL OFFICE SALARIES AND EXPENSES

661. **Executive department.**—This account shall include the pay, office, traveling, and other expenses of officers who are en-

gaged in the general administration or management of the company, or its affairs in a territorial subdivision; also the pay and expenses of their assistants and office forces.

This account shall be charged also with salaries, fees, and expenses other than law expenses, of receivers.

OFFICERS AND EMPLOYEES

[Note instruction 8]

Chairman of the board of directors.
Managers—general and division.
President.
Receiver.
Secretary.
Vice president.
Assistants authorized to act for officers of executive department.
Office and staff forces (e. g., staff assistants, secretaries, stenographers, clerks, messengers, office boys, etc.) of officers and employees of executive department.

EXPENSES AND SUPPLIES

[Note instruction 8]

Automobile service, including charges through clearing account 702.
Books and periodicals for office use.
House service. (Note also account 707.)
Meals, including payments therefor on account of overtime work
Office supplies.
Postage.
Printing.
Repairs of furniture and office equipment, and cost and repairs of individual items of small value or short life.
Stationery supplies.
Telephone and telegraph service, amounts paid others for.
Traveling expenses.

662. **Accounting department.**—This account shall include the pay, office, traveling, and other expenses of officers, their assistants, and office forces, of the accounting department.

OFFICERS AND EMPLOYEES

[Note instruction 8]

Accountants. (See also note to this account.)
Addressograph clerks.
Auditor of disbursements.
Auditor of receipts.
Auditors—general and division.
Billing clerks.
Bookkeepers.
Chief accountant.
Chief statistician.
Chief traveling auditor.
Clerks.
Comptroller.
Divison auditor of disbursements.

Division auditor of receipts.
General accountants.
Office managers. (See also note to this account.)
Plant accountants.
Revenue accountants.
Statisticians.
Supervisors of methods, bookkeeping, vouchers, pay rolls, estimates, etc.
Tax accountants.
Traveling auditors.
Vice president in charge of accounting department.
Assistants authorized to act for officers of accounting department.
Office and staff forces (e. g., staff assistants, secretaries, stenographers, messengers, office boys, etc.) of officers and employees of accounting department.

EXPENSES AND SUPPLIES

[Note instruction 8]

Automobile service, including charges through clearing account 702.
Books and periodicals for office use.
House service. (Note also account 707.)
Meals, including payments therefor on account of overtime work.
Office supplies.
Postage, including that used in mailing bills to customers by accounting department and in forwarding toll tickets to local collection offices.
Printing.
Repairs of furniture and office equipment, and cost and repairs of individual items of small value or short life.
Stationery supplies.
Telephone and telegraph service, amounts paid others for.
Traveling expenses.

NOTE.—The expense of accounting performed by employees of operating departments shall be charged to the appropriate accounts of those departments (e. g., the pay and expense of employees of local business offices engaged in keeping and billing customers' accounts shall be charged to account 645). (Note also instruction 63.)

663. **Treasury department.**—This account shall include the pay, office, traveling, and other expenses of officers, their assistants and office forces, of the treasury department.

OFFICERS AND EMPLOYEES

[Note instruction 8]

Cashiers. (See also note A to this account.)
Clerks.
Office managers.
Paymasters. (See also note A to this account.)
Supervisors of methods, stock and bond records, interest payments, etc.
Stock and bond ledger clerks.
Treasurer.
Vice president in charge of treasury department.
Assistants authorized to act for officers of treasury department.

Office and staff forces (e. g., staff assistants, secretaries, stenographers, messengers, office boys, etc.) of officers and employees of treasury department.

EXPENSES AND SUPPLIES

[Note instruction 8]

Automobile service, including charges through clearing account 702.
Books and periodicals for office use.
House service. (Note also account 707.)
Meals, including payments therefor on account of overtime work.
Office supplies.
Postage.
Printing, including stock and bond certificates for transfer purposes. (See also note B to this account.)
Repairs of furniture and office equipment, and cost and repairs of individual items of small value or short life.
Stationery supplies.
Telephone and telegraph service, amounts paid others for.
Traveling expenses.

NOTE A.—The pay and expenses of cashiers and paymasters employed by operating departments shall be charged to the appropriate accounts of those departments.

NOTE B.—The cost of printing stock certificates in connection with original and additional capital stock issues shall be charged to account 134.2, and the cost of printing bonds in connection with new or additional issues of long-term debt shall be accounted for as provided in instruction 15.

664. **Law department.**—This account shall include, when not provided for elsewhere, the pay, office, and other expenses of officers, their assistants and office forces, and other employees of the law department, the cost of suits and other law costs, including law expenses connected with damages.

OFFICERS AND EMPLOYEES

[Note instruction 8]

Attorneys.
Claim agents, investigators, and adjusters. (See also note A to this account.)
Clerks.
Counsel.
General attorney.
General counsel.
General solicitor.
Law agents.
Law clerks.
Librarians.
Patent attorneys.
Solicitors.
Special counsel.
Tax attorneys.
Vice president in charge of law department.
Assistants authorized to act for officers of the law department.
Office and staff forces (e. g., staff assistants, secretaries, stenographers, messengers, office boys, etc.) of officers and employees of law department.

EXPENSES AND SUPPLIES

[Note instruction 8]

Automobile service, including charges through clearing account 702.
Agreements, briefs, contracts, legal forms and reports, cost of preparing and printing.
Collecting revenue and other accounts, law expenses in connection with.
Court expenses.
Depositions, cost of taking.
Examination of titles and other expenses incurred in suit to test validity of bond issue. (See also note B to this account.)
Fees and retainers of attorneys not regular employees.
Filing tax reports, passing tax claims, making returns to tax assessors, etc., cost of when handled by law department.
House service. (Note also account 707.)
Law books and periodicals.
Law expenses in connection with rate cases or filing or adjustment of rate schedules.
Law expenses of receivers.
Meals, including payments therefor on account of overtime work.
Office supplies.
Postage.
Premiums on surety bonds.
Printing.
Repairs of furniture and office equipment, and cost and repairs of individual items of small value or short life.
Special fees.
Stationery supplies.
Telephone and telegraph service, amounts paid others for.
Testimony, cost of printing and transcripts of.
Traveling expenses.
Witness fees.

NOTE A.—The pay and expenses of claim agents, investigators, and adjustors employed by departments other than the law department shall be charged to the accounts of the department by which they are employed.

NOTE B.—Special law expenses incurred incident to the construction of telephone plant shall be charged to the appropriate telephone plant accounts; special law expenses incident to the issuance of capital stock and long-term debt shall be accounted for as provided in instruction 15 and account 134.2.

665. **Other general office salaries and expenses.**—This account shall include the pay, office, traveling, and other expenses of officers, their assistants, and office forces of general offices not properly chargeable to other accounts, such as those engaged in editing magazines or periodicals published in behalf of all departments and employees engaged in detective or protective services for the company's interest as a whole.

EXPENSES AND SUPPLIES

[Note instruction 8]

House service. (Note also account 707.)
Meals, including payments therefor on account of overtime work.

Office supplies.
Postage.
Printing, including cost of printing magazines or periodicals published in behalf of all departments.
Repairs of furniture and office equipment, and cost and repairs of individual items of small value or short life.
Stationery.
Traveling expenses.

NOTE.—The expenses of miscellaneous general activities when incidentally performed by employees of operating departments shall be included in the accounts of those departments. (Note also instruction 63.)

VI. OTHER OPERATING EXPENSES

668. Insurance.—(A) This account shall include the cost, not provided for elsewhere, of commercial insurance to protect the company against losses and damages in its telephone operations. (Note also account 131.)

To this account shall be charged:

(1) The amount of insurance premiums paid to insurance companies.

(2) Special costs incurred in procuring insurance, such as brokerage fees, notarial fees, and insurance inspection service, and the pay, traveling, and office expenses of officers, clerks, and other employees of an insurance department.

(B) This account shall include also amounts credited to account 169, "Insurance reserve", for self-carried risks as provided in paragraph (B) of that account.

(C) This account shall include also the amount of insurance premiums covering blanket policies for which there is not available an equitable basis for allocation to the several accounts which may be involved.

(D) A list of representative losses and damages follows, the insurance premiums for protection against which are chargeable to this account when incurred in connection with the company's telephone operations:

LOSSES AND DAMAGES

[Note instruction 8]

Burglaries, holdups, check alterations, and forgeries.
Damages to the property of others.
Defalcations of employees and agents.
Fire and other casualties to telephone plant.
Fire and other casualties to telephone plant rented to others, the rents from which are includible in account 524.
Injury to or death of employees.
Injury to or death of persons other than employees.
Loss due to business interruption (i. e., use and occupancy insurance).
Loss of service of employees through death, sickness, injury, or other cause.

Loss of unbilled toll tickets.
Nonperformance of contractual obligations of others.

NOTE.—All losses and damages, sustained, including those covered by commercial insurance or reserves carried in account 169 shall be charged to the depreciation reserve, construction, repair, accident and damages, or other appropriate account, according to the character of the losses. Insurance recoverable or chargeable to account 169 on account of losses and damages sustained shall be credited to the account to which the losses and damages are chargeable.

669. **Accidents and damages.**—(A) This account shall include expenses, not provided for elsewhere, on account of persons killed or injured and property of others damaged in connection with the company's telephone operations.

(B) When an admitted liability arises because of an accident or damage, any portion of such liability, estimated if not known, chargeable to this account (i. e., the amount in excess of the liability insured) shall be charged hereto and credited to account 174, "Other deferred credits." When an estimated liability has been so charged to this account, appropriate adjustments between this account and account 174 shall be made when the extent of the liability has been definitely ascertained. (Note also account 174 and instruction 4.)

(C) This account shall be credited and the appropriate property account charged with the amount of such accidents and damages due to construction work. (Note also instruction 22–B–6.)

(D) Accident and damage payments provided for by commercial insurance or by a reserve for self-carried risks shall be credited to this account and charged to the insurer or to the reserve carried in account 169, "Insurance reserve", as appropriate.

ITEMS

[Note instruction 8]

Amounts paid in settlement of personal injury or damage claims.
Damage payments resulting from errors in directory listings, directory advertising errors, and traffic service errors. (See also note A to this account.)
Damage to property of others, cost of. (See also note B to this account.)
Fees and expenses of surgeons, doctors, coroners, and undertakers.
Nursing, hospital attendance, and medical and surgical supplies, cost of. (See also note C to this account.)

NOTE A.—Refunds of revenue overcharges in connection with such errors shall be charged to the revenue accounts originally credited.

NOTE B.—The cost of incidentally repairing property of others damaged in the course of maintenance or construction work shall be included in the cost of the work.

NOTE C.—Payments to or on behalf of employees, including accident and death benefits, salary, hospital attendance and medical supplies; also salaries, fees and expenses of surgeons, doctors, and nurses, etc., shall

be charged to account 672 when coming within the scope of a company's general provision for employees' benefits.

NOTE D.—The pay and expenses of employees performing services in the investigation and adjustment of accident and damage claims shall be included in the accounts of the department by which such employees are employed.

671. **Operating rents.**—(A) This account shall include rents payable for the use of space in buildings occupied by the company, space in conduits, pole line space for attachments, instruments, equipment, and other telephone plant, the rent for which is not provided for elsewhere.

(B) This account shall include also taxes borne by the lessee of property, the rent for which is chargeable to this account.

ITEMS

[Note instruction 8]

Rents for location of poles, conduits, or cables.
Rents for use of general offices and central and branch telephone offices except rents chargeable to the clearing accounts.
Rents for use of ducts, conduits, and subways.
Rents for use of poles and buildings as supports for telephone circuits.
Rents for telephone instruments and equipment.
Rents for use of circuits.

NOTE A.—Expenses incurred by the company in maintaining and operating property, the rent for which is includible in this account, shall be charged to the operating expense account appropriate for owned property.

NOTE B.—This account shall not include rents provided for in the clearing accounts and in instruction 22–B.

NOTE C.—Rents for the exclusive use of telephone operating property held as a whole and operated by the company, such as a complete telephone plant, a complete exchange, or a complete toll system, shall be included in account 303.

NOTE D.—The accounting for amortization of leaseholds and similar intangible telephone property carried in account 211 shall be as provided in account 613.

672. **Relief and pensions.**—(A) This account shall include pensions or other benefits paid to active and retired employees, their representatives or beneficiaries, and salaries and expenses incurred in conducting relief, benefit, and general medical departments. It shall include payments to or on behalf of employees on account of injuries or accidental death when such payments come within the scope of a company's general provision for employees' benefits.

(B) If the company has definitely undertaken by contract to pay pensions to employees when regularly retired for superannuation or disability and has established a fund to be held in trust for such pension purposes, the company shall charge to this account monthly amounts determined through the application of equitable actuarial

factors to the current pay rolls, which, together with interest accruals on the trust funds, will as nearly as may be, provide for the payment of such pensions, or for the purchase of annuities corresponding thereto. The amounts so charged shall be concurrently credited to a separate subaccount under account 170, "Provident reserve." The amounts accrued in each year shall correspond to the aggregate of the amounts expended directly by the company for pensions or annuities during the year and amounts paid into the trust fund. The company shall maintain a complete record of the actuarial computations through which the accrual each month of its pension liabilities is established.

(C) Upon the adoption of the accrual plan of accounting, pension payments to employees retired before the adoption of such plan shall be charged to an existing pension reserve or to account 413, "Miscellaneous debits to surplus." If a company pays into its pension trust fund the amount of its existing pension reserve, any such amounts in excess of provision for pensions granted prior to the adoption of the accrual plan may be applied in whole or in part to the adjustment of future accrual charges.

(D) Before adopting the accrual plan of accounting for pensions the company shall inform this Commission of the details of its pension plan giving full statement of the facts which in its judgment establish a contractual obligation for pension payments together with the actuarial formula under which it proposes to create its pension trust fund, and also a copy of the declaration of trust under which the fund is established.

(E) No charges to this account shall be made in anticipation of discretionary pension payments in the future.

(F) This account shall include also, under a separate subaccount, amounts accrued to provide for the payment of termination allowances or similar benefits to employees of the company when such employees are laid off because of lack of work, and to provide necessary and warranted relief to former employees. Charges to this subaccount shall be made only after approval by this Commission of the company's plan for administering payments for these purposes and of the amount of the accruals. Amounts charged to this subaccount shall be concurrently credited to account 173, "Employment stabilization reserve."

(G) There shall be credited to this account that portion of each class of relief and pensions assigned to construction, plant removal, and custom work labor.

ITEMS

[Note instruction 8]

Accident, sickness, death, and other disability benefits to employees, their representatives or beneficiaries.

Employees of relief, benefit, and general medical departments, pay and expenses of.

Expenses in connection with employees' disability cases, such as hospital, nursing, and medical attendance.
Fees and retainers for medical and similar services incurred by relief, benefit, and general medical departments.
House service. (Note also account 707.)
Medical supplies.
Office supplies.
Postage, printing, and stationery.
Premiums paid for group insurance for the benefit of employees or their beneficiaries.
Repairs of furniture and equipment, and cost and repairs of individual items of small value or short life.
Traveling expenses.

673. **Telephone franchise requirements.**—(A) This account shall include the cost not provided for in account 202, "Franchises", of all services, plant, material and supplies, and similar items, including standard rates for telephone services, furnished to municipalities or other governmental authorities in compliance with franchises, ordinances, or similar requirements and for which no reimbursement or payment is received by the company. (See also note A to this account.) It shall include the cost of paving and of premiums on bonds required under the general terms of a franchise or ordinance and not in connection with specific construction or maintenance work.

(B) This account shall include also amounts paid for franchises running for 1 year or less after acquisition and may include direct charges for franchises acquired at small cost.

(C) Amounts charged to this account involving no direct money outlay, such as standard rates for telephone service rendered without charge, shall be credited to account 676, "Telephone franchise requirements—Cr."

NOTE A.—The cost of plant, supplies, etc., given as an initial consideration for a franchise running for more than 1 year shall be charged to account 202.

NOTE B.—Franchise taxes paid annually or more frequently shall be charged to account 305.

NOTE C.—The cost of plant used by a municipality without charge, or used by the company in rendering services to a municipality without charge, shall be included in the appropriate telephone plant accounts; maintenance expenses incurred in connection with such plant shall be charged to the appropriate maintenance accounts.

NOTE D.—The cost of reconstructing or changing the location of plant to conform with municipal requirements, including such work required under the provisions of a franchise or ordinance, shall be charged to the maintenance, telephone plant, and depreciation reserve accounts appropriate for the work performed.

NOTE E.—The accounting for amortization of limited term franchises carried in account 202 shall be as provided in account 613.

674. **General services and licenses.**—This account shall include amounts payable for services received under a license agreement, a general service contract, or other arrangement providing for the

furnishing of general accounting, engineering, financial, legal, patent, and other general services.

675. **Other expenses.**—This account shall include all operating expenses not properly chargeable to other accounts.

ITEMS

[Note instruction 8]

Amounts paid for patents having an estimated service life of 1 year or less and patents acquired at small cost.
Commissions paid agents for leasing space to others in buildings partly occupied by the company in connection with its telephone operations.
Cost of publishing reports to stockholders, notices of stockholders' meetings, election of directors, conversion of bonds, and dividends declared.
Cost of valuations, inventories, and appraisals of telephone plant made for rate case purposes, and those taken in compliance with orders of Federal, State, or other regulatory authorities. (See also notes B and C to this account.)
Fees and expenses of directors.
Fees of agents for registrations and transfers of outstanding capital stock.
Franks for use of officers and employees, cost of printing.
General audit of company's books by audit company, cost of.
House service furnished for space leased to others when not specifically reimbursed.
Losses from foreign exchange. (Note also instruction 7.)

NOTE A.—The accounting for amortization of patents carried in account 203 shall be as provided in account 613.

NOTE B.—The cost of valuations, inventories, and appraisals taken in connection with the contemplated purchase or sale of property shall be charged to account 139 pending further disposition.

NOTE C.—The pay and expenses of officers and employees performing incidental services in valuations, inventories, and appraisals shall be included in the accounts ordinarily charged with their pay and expenses. (Note also instruction 63.)

676. **Telephone franchise requirements—Cr.**—This account shall be credited with amounts charged to account 673, "Telephone franchise requirements", for which there is no direct money outlay, such as standard rates for telephone service furnished without charge to municipalities in accordance with franchise requirements.

677. **Expenses charged construction—Cr.**—This account shall be credited and the appropriate construction accounts charged with amounts, not provided for elsewhere, representing the portion of operating expenses applicable to construction work. (Note also instruction 22–B.)

CLEARING ACCOUNTS

(Note particularly instructions 2–C and 70)

702. Vehicle and other work equipment expense.
704. Supply expense.
705. Engineering expense.
706. Plant supervision expense.
707. House service expense.

702. **Vehicle and other work equipment expense.**—(A) This account shall include the expense of operating vehicles and other work equipment, including the expenses of garages, shops, toolrooms, and stables and the amount of depreciation charges applicable to the accounting period for plant classified in account 264, "Vehicles and other work equipment", except equipment of storerooms.

(B) This account shall be cleared by adding to the cost of work performed such amounts as will distribute the total expense equitably. (Note also account 602.9.)

ITEMS

[Note instruction 8]

Books and periodicals.
Depreciation of vehicles and other work equipment, except equipment of storerooms.
House service. (Note also account 707.)
Insurance (see also note to account 668), including that against losses and damages to or by vehicles and other work equipment.
License fees for vehicles and for drivers.
Office supplies.
Overages and shortages in material and supplies for vehicles and other work equipment.
Postage, printing, and stationery.
Rent paid for and repairs of rented vehicles and other work equipment, garages, shops, toolrooms, stables, and other quarters. (Note also instruction 23.)
Repairs of furniture and office equipment, and cost and repairs of individual items of small value or short life.
Repairs of vehicles and other work equipment, and cost and repairs of individual items of small value or short life.
Supplies, such as feed, fuel, gasoline, oil, tires, tubes, tire chains, soap, waste, sponges, measures, funnels, electric power, etc., used in the operation of vehicles and other work equipment, garages, shops, toolrooms, and stables.

Supervising officers and their office and field forces, including inspectors, testers, garagemen, and other employees, pay and expenses of.

704. **Supply expense.**—(A) This account shall include the expenses incurred in connection with the purchase, storage, handling, and distribution of material and supplies which are not allocated to other accounts as incurred; and the amount of depreciation charges applicable to the accounting period for equipment of storerooms.

(B) This account shall be cleared by adding to the cost of material and supplies a suitable loading charge which will distribute the total expense equitably.

ITEMS

[Note instruction 8]

Books and perodicals.
Depreciation of equipment of storerooms.
Discounts on material, cash and other. (See also note A to this account.)
House service. (Note also account 707.)
Overages and shortages in material and supplies which cannot be assigned to specific accounts. (Note also accounts 122 and 702.)
Insurance (see also note to account 668), including that against losses and damages to material and supply stock.
Losses due to depreciation, breakage, leakage, evaporation, and fire and other casualties to supply stock not assigned to specific accounts nor distributed through the pricing of materials and supplies disbursed.
Office supplies.
Postage, printing, and stationery.
Purchasing agents, superintendents and supervisors of supplies, managers of stores, storekeepers, clerks, and laborers, pay and expenses of.
Rent paid for and repairs of rented storehouses, storerooms, storage yards, and other quarters. (Note also instruction 23.)
Repairs of furniture and office equipment, and cost and repairs of individual items of small value or short life.
Transportation charges, undistributed. (See also note B to this account.)
Traveling expenses.

NOTE A.—So far as practicable, cash and other discounts on material shall be deducted in determining the cost of the particular material to which they relate or credited to the account to which the material is charged.

NOTE B.—Transportation charges on material purchased shall be, so far as practicable, included as a part of the cost of the particular material to which they relate. Transportation charges on material recovered from plant shall be charged to the account to which the cost of removal is charged.

705. **Engineering expense.**—(A) This account shall include the expenses of the general engineering department.

(B) This account shall be cleared by apportioning the total expenses to the appropriate accounts on the basis of service

rendered, as determined by the time devoted to particular jobs. (Note also account 602.9.)

ITEMS

[Note instruction 8]

Books and periodicals.
Engineering officials and employees, pay and expenses of.
House service. (Note also account 707.)
Office supplies.
Postage, printing, and stationery.
Rent paid for and repairs of rented offices. (Note also instruction 23.)
Repairs of furniture and office equipment, and cost and repairs of individual items of small value or short life.
Tools and instruments of small value or short life.
Traveling expenses.

NOTE.—Expenses included in this account, incurred in connection with projects which are abandoned, shall be cleared to account 413. (Note also account 139.)

706. **Plant supervision expense.**—(A) This account shall include the expense of general supervision of the maintenance and construction of the plant where a department of the company's organization is charged with both maintenance and construction.

(B) This account shall be cleared on the basis of labor supervised except that charges for plant engineering shall be cleared by charges to the appropriate accounts on the basis of the time devoted to particular jobs. (Note also account 602.9.)

ITEMS

[Note instruction 8]

Books and periodicals.
House service. (Note also account 707.)
Office supplies.
Plant supervising officers and their staffs, including engineers, office and field forces charged with planning for and superintending the work of maintenance and plant construction, pay and expenses of. (See also note to this account.)
Postage, printing, and stationery.
Rent paid for and repairs of rented offices. (Note also instruction 23.)
Repairs of furniture and office equipment, and cost and repairs of individual items of small value or short life.
Traveling expenses.

NOTE.—The pay and expenses of foremen in direct charge of jobs, general foremen and other supervisory employees not engaged in the general supervision of maintenance, construction, and plant removals, such as local plant administrative employees whose duties are limited as to functions or areas shall be included in the cost of the work supervised and not charged to this account.

707. **House service expense.**—(A) This account shall include the expenses of operating offices and buildings, whether owned or

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rented, when such expenses are not allocated, as they are incurred, to the operating expense and other accounts.

(B) This account shall be cleared by apportioning the entire expense to the operating expense and other accounts on the basis of the use made of such property.

ITEMS

[Note instruction 8]

Building superintendents and others engaged in supervising house service operations, pay and expenses of.
Cleaning supplies.
Elevator service.
Fuel.
Heat.
Janitor service.
Light.
Office supplies.
Postage, printing, and stationery.
Power. (Note also accounts 604 and 610.)
Refrigeration.
Rent paid for and repairs of rented quarters used in the supervision of general house service operations, other than space used by janitors and similar employees in furnishing house service for a particular building. (Note also instruction 23.)
Repairs of furniture and office equipment, and cost and repairs of individual items of small value or short life.

APPENDIX A

UNITS OF PROPERTY

The following list of units of property shall be used in connection with the accounting provided in instructions 24 and 25, but shall not be considered as determining the classification of the telephone plant involved.

212. **Buildings.**

A complete building.

An entire roof with or without supporting members.

NOTE A.—A building of irregular shape having more than one roof level may have several isolated roofs, each of which shall be considered an entire roof. In the case of buildings to which lateral extensions have been made, even though having but one roof level, that part of the roof covering an entire section built at one time shall be considered an entire roof.

A complete fire escape.

A complete metal window (I. e., box, frame, and sash).

A boiler, furnace, hot-water heater, or automatic stoker.

A coal or ash conveying system.

An elevator complete with operating mechanism.

A gas-burner system.

A house-lighting or power board.

An oil-burner system.

An oil tank.

The floor covering for one room.

A motor, generator, engine, turbine, pump, compressor, ventilating fan, air washer, elevator drum, or similar item of equipment, with or without associated wiring, control equipment, etc.

NOTE B.—In addition to the above units of property, material (I. e., portions of buildings, equipment, fixtures, etc.) installed and retired, and the labor and incidental costs involved in connection with work of the following character, shall be handled through the telephone plant and depreciation reserve accounts:

(1) Changes in the type of operation of elevator systems, e. g., a change from manual to signal control of cars, from manual to power operation of doors, from low speed to high speed, from direct to alternating current, from hydraulic to electric operation, from one type of signaling or dispatching system to another.

(2) Relocations of toilet rooms, battery rooms, kitchens, terminal rooms, machine rooms, transformer vaults, etc.

(3) Structural changes such as: (a) Reinforcements of floors, roofs, bearing walls, footings, and foundations; (b) additions or relocations of elevator shafts, stairways, fire exits, and vaults, but excluding switchboard cable holes and slots; and (c) building alterations required for fire protection and other safety measures.

(4) Changes in the type of electric current supply, or of ventilating, air conditioning, or similar systems.

(5) Building enlargements.

(6) Replacements of the following character—

(a) Replacements of plumbing or heating pipes (with or without associated valves) except when necessitated by minor repairs or minor relocations of fixtures.

(b) Replacements of all or substantially all of the lighting fixtures (with or without associated wiring and conduit) in one operating or equipment room or, in the case of office space, on one floor of a building.

(c) General replacements (throughout a building or throughout an entire portion erected at one time) of items such as supply, return, or air valves in heating systems; hot or cold water valves or faucets; plumbing, heating, or drainage traps.

221. Central Office equipment.

Switchboards, desks, and testboards—

Switchboards (i. e., local, toll, dial system "A", cordless "B", call distributing "B", observing, teletypewriter, etc.)—A complete section or lower unit.

Desks (i. e., operating, observing, testing, etc.)—A complete section.

Testboards, or test and control boards (board type)—A complete section.

Testboards, or test and control boards (rack type)—

All the equipment in one bay.

A complete upper unit.

A complete lower unit.

A complete installation of rack framework for one board.

Test panels—A complete panel.

Test cabinets—A cabinet complete with equipment.

Distributing frames—

Main distributing frames (including wall type)—A complete installation for one central office (in multi-unit offices, for one operating unit).

Intermediate distributing frames—A complete installation for one central office (in multi-unit offices, for one operating unit).

Mezzanine balconies—A complete installation for one frame.

Racks—

Relay rack equipment—

A panel or unit complete with equipment.

All the equipment in one bay, exclusive of any panels or units.

221. **Central Office equipment.**—Continued.

Racks—Continued.

Coil rack equipment—All the equipment on one shelf.

Message and traffic register rack equipment—All the equipment in one bay.

Iron framework—A complete line of rack with or without enclosing cabinet or case.

Cable—

All of the cables in one run used for the same purpose, such as between—

(1) Main frame and intermediate frame for subscribers' lines.

(2) Main frame and intermediate frame for outgoing trunk multiple.

(3) Intermediate frame and connector frame or final frame for subscribers' lines.

(4) Intermediate frame and answering jacks.

(5) Intermediate frame and switchboard for outgoing trunk multiple jacks.

(6) Intermediate frame and switchboard for subscribers' multiple jacks.

Iron framework—A complete installation of rack for one cable run.

Power equipment—

Frame or rack mounted equipment—

A panel or shelf complete with equipment, such as fuses, meters, control equipment, etc.

Iron framework—A complete line of frame or rack for one fuse board, one power switchboard, etc.

A generator, motor, motor generator set, gas engine, rectifier, ringing machine, harmonic converter, pole changer, interrupter, power filter, or choke coil.

Storage batteries:

A complete battery with or without rack, cabinet, or counter electric motive force cells.

All positive or all negative plates in an entire battery (i. e., in all cells of a 24-volt battery, in all cells of a Morse battery, etc.).

All tanks or all jars of an entire battery.

A complete battery rack or cabinet, storage or dry.

A complete group of bus bars, cable, or wiring (with or without conduit) such as between—

Battery and fuse panel.

Power switchboard and machines.

Telephone repeater equipment (including testing equipment)—

A complete floor mounted rack type set.

221. **Central Office equipment.**—Continued.

Telephone repeater equipment (including testing equipment)—Continued.

Relay rack mounted equipment—

A panel or unit, complete with equipment.

All the equipment in one bay, exclusive of any panels or units.

Coil rack mounted equipment—All the equipment on one shelf.

Iron framework—A complete line of rack.

Carrier equipment (telephone, telegraph, repeater, and testing equipment)—

A complete floor mounted rack type set.

Relay rack mounted equipment—

A panel or unit complete with equipment.

All the equipment in one bay, exclusive of any panels or units.

A line filter.

A complete test table.

Iron framework—A complete line of rack.

Telegraph equipment (printer and manual)—

Telegraph testboards—A complete section or bay.

Duplex, single line telegraph, and polar repeaters—A table or bay complete with equipment.

Metallic telegraph repeaters—

A complete floor mounted rack type set.

A panel or unit complete with equipment.

Voice frequency carrier equipment—A panel or unit complete with equipment.

Voice frequency carrier battery supply apparatus—

A complete bay of equipment.

A complete test table.

Iron framework—A complete line of rack.

Telephotograph equipment—

Table-mounted sending or receiving equipment—

A table complete with equipment.

A complete optical system.

A complete mechanical system.

A complete fork box.

A complete amplifier-modulator box.

Rack-mounted sending or receiving equipment—

A panel complete with equipment.

All the equipment in one bay.

Iron framework—A complete line of rack.

Power equipment—

A complete power board.

A complete storage battery.

221. Central Office equipment.—Continued.

Telephotograph equipment—Continued.

Photographic equipment—

A copying camera or a copying, enlarging, and reducing camera, each with or without associated stands, illuminators, and copy boards.

A print machine.

A drying cabinet.

A developing, fixing, and washing tank.

Radio equipment—

A complete transmitter.

Miscellaneous equipment—

A calculagraph, a master clock, or a secondary clock.

Electrically driven calculagraph and clock systems—A complete installation.

Mechanical or pneumatic tube ticket distributing system—A complete installation.

Each complete tool or portable test set the original cost of which was charged to the telephone plant account, such as a plug remover and attacher, cam aligning fixture, multiple bank resetting gage, or shaft straightening tool, a relay adjusting set, line finder set, or wagon type set.

Each complete item of furniture or other miscellaneous equipment, the original cost of which was charged to the telephone plant account, such as a desk or table equipped with central office equipment, an operator's chair, a complete switchboard platform, an operator's telephone set cabinet, a rotary file or directory cabinet, a ticket cabinet or rack, a tarpaulin with or without cabinet, a portable service-observing cabinet, or a holding-time recorder.

Loud-speaker equipment—A complete installation.

Aisle-lighting equipment—A complete installation on one floor.

Rolling ladders—A complete installation for one side of one frame or rack.

Message and traffic register cabinets—A cabinet complete with equipment.

Teletypewriter sets—Units specified under account 231.

Panel dial system equipment—

A complete equipment frame such as line-finder frame, line-switch frame, selector frame, link frame, routine test frame, decoder frame, sender frame, or floor alarm board.

221. Central Office equipment.—Continued.

Panel dial system equipment—Continued.

Pulse-machine equipment—A complete pulse machine.

Pulse-machine control apparatus—A complete installation controlling a set of pulse machines.

Step-by-step dial system equipment—

A complete equipment frame, such as a line-finder frame, line-switch frame, selector frame, connector frame, or repeater frame.

Key-indicator equipment or key-pulsing equipment—

A complete equipment frame, such as a link or sender frame.

NOTE.—When work of the following character is performed as a special job in a central office or at a multiple or dial private branch exchange for the purpose of improving or changing the type of the equipment, the material installed and retired and the labor and incidental costs involved shall be handled through the telephone plant and depreciation reserve accounts.

(1) Conversions of one or more switchboard positions, or dial-system frames, from one type to another, such as from subscribers' to toll, subscribers' to rural, inward toll to combined line and recording, manual B to call indicator B, or from panel B switchboard incoming frame to interoffice incoming frame.

(2) Conversions of circuits from one type to another, such as conversions of cord circuits from two-party ringing to four-party selective ringing, semiselective ringing to selective ringing, or from manual recall to flashing recall, and conversions of panel-sender circuits from noncoin to coin and from two digit to three digit.

(3) Replacements of items of one type with items of a different type for such reasons as improving signaling or transmission characteristics, changing operating methods or increasing capacity of the office, e. g.:

(*a*) Replacements of all the relays or repeating coils of one type in a central office with relays or coils of an improved type for the purpose of improving the signaling or transmission characteristics.

(*b*) Replacements of items of equipment in dial offices because of a change in the method of operation to multiple registration.

(*c*) Replacements of items of power equipment because of a change in power purchased from direct current to alternating current.

(*d*) Modifications of the trunk and cord circuits of multiple manual private branch exchange boards necessitated by a cutover of a central office district to dial operation.

(*e*) Replacements of protectors of one size with protectors of a smaller size on a main distributing frame so that more protectors may be installed in the same space.

(*f*) Replacements of 20 pair terminal strips on a main distributing frame with 50 pair strips to increase the capacity of the frame.

(*g*) Replacement of jack strips having 10 jacks per strip with strips having 20 jacks per strip to increase the capacity of a switchboard.

(*h*) Replacement of keys of one type with keys of a different type to permit more keys to be placed in the same position.

231. Station apparatus.

A complete station.
A desk stand, with or without transmitter, receiver, or dial.
A hand set (i. e., transmitter, receiver and handle).
A hand set mounting, with or without dial.
A wall set, with or without transmitter, receiver, or dial.
A bell box or other subscriber set, such as extension bell, signal horn, etc.
A coin collector, with or without transmitter, receiver, or dial.
A complete apparatus cabinet.
A complete key cabinet or key box.
An intercommunicating system key.

NOTE.—The original cost less salvage of the following items of station apparatus not designated units of property shall be charged to the depreciation reserve account when lost, destroyed, junked, or otherwise disposed of:

A hand-set handle.
A transmitter.
A receiver.
A dial.
A dial mounting.
A switching key (individually mounted type).

Teletypewriter equipment—

A complete station.
A printer or teletypewriter.
A printer or teletypewriter table or stand.
A base (printer or reperforator).
A cover (printer or reperforator).
A printer unit or typing unit.
A keyboard unit.
A distributor unit.
A transmitter unit.
A perforator unit.
A reperforator unit.
A relay box with equipment.
A motor or motor unit (excluding the motor of a motor generator set).
A motor generator set.
A rectifier unit.
A loop switchboard.
A station signaling set.

281. **Station apparatus.**—Continued.

Manual telegraph equipment—

A complete station.

A loop switchboard.

Program supply and public address equipment—

A microphone transmitter.

A microphone transmitter mounting.

An amplifier.

A loud-speaking receiver.

A horn.

An observer's telephone set.

A complete dynamotor, motor generator, rectifier, or storage battery.

A complete control cabinet, resistor cabinet, or junction box.

A battery cabinet.

Rack mounted equipment:

All the equipment in one bay.

A panel complete with equipment.

Iron framework—A complete line of rack.

Portable equipment—A complete item of portable equipment, with or without the carrying case (e. g., an amplifier, a transmitter mixing panel, an oscillator, or an equalizer).

Radio receiving sets and equipment associated therewith—A complete installation.

232. **Station installations.** (Note instruction 25, paragraph B.)

233. **Drop and block wires.** (Note instruction 25, paragraph B and account 605.)

234. **Private branch exchanges.**

A complete cordless or nonmultiple switchboard, with or without local storage batteries or cables classified as P. B. X. equipment.

An apparatus cabinet as used with certain nonmultiple boards.

A complete section of an order-receiving table.

An order turret (not including the turrets forming part of an order-receiving table).

An attendant's cabinet complete with equipment.

A code sending set or code call unit.

A complete teletype switchboard.

An operator's chair.

Multiple private branch exchange equipment and private dial system equipment (except as provided below)—Units specified under account 221, "Central office equipment."

234. Private branch exchanges.—Continued.

An equipment cabinet complete with batteries and switching equipment mounted therein, as generally used with a dial system installation of small capacity.

Local storage battery plants of the type used to serve several nonmultiple boards or of the type used with certain small multiple P. B. X. installations—An entire battery with or without cabinet or control apparatus.

Local automatic power plants of the type used to serve a small dial or a small multiple P. B. X.—

A control cabinet, with or without charging or ringing equipment.

An entire battery, with or without cabinet or counter E. M. F. cells.

235. Booths and special fittings.

A booth compartment, with or without special fittings or associated furniture and fixtures such as chairs, directory racks, directory tables, and counters.

An attendant's desk including equipment or a switchboard.

241. Pole lines.

A pole (i. e., line pole, brace pole, guy stub, or pole forming part of A or H fixture), a pole stub, or a pole butt, with or without associated anchors, guys, steps, etc.

A crossarm (i. e., wooden crossarm, guard arm, or cable crossarm, including extension arms), with or without associated braces and other hardware.

A special fixture (i. e., a bridge fixture, a tower or other special river-crossing or long-span fixture), with or without associated anchors, guys, etc.

242.1. Aerial cable.

242.2. Underground cable.

242.3. Buried cable.

242.4. Submarine cable.

A span of cable, with or without associated suspension strand, clamps, rings, etc. (The term "a span" shall include a length of cable from a "Y" splice not located at a pole to a pole or building.)

A section or run of cable, with or without associated elements and parts, as follows:

(1) Between a manhole, handhole, or service box and a pole, building, fence, wall, or the junction with house cable.

(2) Between manholes, handholes, or service boxes; or between an office cable vault and an office manhole.

242.1.
242.2.
242.3.
242.4.
Aerial cable, etc.—Continued.

A section or run of cable, etc.—Continued.

(3) Between a cable vault or an office manhole and the junction with the main frame terminating cables.

(4) A section of buried cable 300 feet or more in length, or a section of buried cable between manholes, splicing boxes, or pedestals.

(5) All of a continuous run of one size of house cable. ("All of a continuous run of one size" means a section between splices other than straight splices.)

(6) All of a continuous run of one size of block cable, i. e., cable attached to buildings, walls, or fences. ("All of a continuous run of one size" means a section between splices other than straight splices.)

(7) All of a submarine cable for one crossing; or a section of submarine cable 300 feet or more in length.

(8) A section of underground dip cable between poles and/or buildings, or the appropriate units listed above.

Any length of cable which is a continuation of a unit of cable and is replaced with such unit.

Any length of cable connected with but not a part of a terminal, or a case of equipment such as loading coils when replaced with the terminal or case of equipment.

Main frame terminating cables (generally silk and cotton insulated)—All the cables including forms used for terminating one outside cable.

A complete cable terminal, protected or unprotected, with or without associated balcony, pole seat, pedestal, etc.

A pressure contactor terminal, with or without contactor.

A house cable terminating frame.

A submarine cable hut or house.

A submarine cable anchorage.

A submarine cable terminating frame.

A fuse pot.

A case of equipment such as loading coils, building-out condensers, carrier line filters, or auto-transformers.

243. **Aerial wire.**

Two continuous spans or more of one wire, with or without associated insulators, transposition brackets, etc.

248. **Aerial wire**—Continued.

A case of equipment such as loading coils, building-out condensers, carrier line filters, or auto-transformers.

An antenna, complete with or without supports.

244. **Underground conduit.**

A section of conduit—

(1) Between two manholes, handholes, or service boxes.

(2) Between a manhole, handhole, or service box and a pole or building.

(3) Between a central office cable vault and an office manhole.

(4) Underground dips—between two poles; between a pole and a building; between two buildings; or units (1) and (2) above.

A manhole, handhole, or service box.

NOTE.—When a manhole is reconstructed, i. e., enlarged or changed in design, the investment representing portions of the manhole removed, whether or not replaced, should be written off to the depreciation reserve account.

261. **Furniture and office equipment.**

Each complete item of furniture or equipment, the original cost of which was charged to the telephone plant account, such as—

A desk, chair, table, piano, davenport, typewriter, computing machine; a section of bookcase, filing cabinet, shelving, bins, or counter; a rug, a carpet, or other floor covering for one room.

264. **Vehicles and other work equipment.**

Each complete item of equipment, the original cost of which was charged to the telephone plant account, such as—

A passenger automobile or truck with or without body; a tractor; a pole jack, splicer's tent or extension ladder; a pole derrick, power winch, earth boring machine, or trailer; a portable test set; a wire measuring machine.

[fol. 236] IN UNITED STATES DISTRICT COURT

[Title omitted]

NOTICE OF APPEARANCE OF OHIO ASSOCIATED TELEPHONE COMPANY, INDIANA ASSOCIATED TELEPHONE CORPORATION, MICHIGAN ASSOCIATED TELEPHONE COMPANY, SOUTHWESTERN ASSOCIATED TELEPHONE COMPANY, INTERSTATE TELEPHONE COMPANY, TRI-STATE ASSOCIATED TELEPHONE CORPORATION, PENNSYLVANIA TELEPHONE CORPORATION, ADDITIONAL PLAINTIFFS—Filed December 6, 1935.

To the Judges of the District Court of the United States for the Southern District of New York:

[fol. 237] Please take notice that in accordance with the provisions of the Code of Laws of the United States, Title 28, Section 45 (a), Ohio Associated Telephone Company, Indiana Associated Telephone Corporation, Michigan Associated Telephone Company, Southwestern Associated Telephone Company, Interstate Telephone Company, Pennsylvania Telephone Corporation and Tri-State Associated Telephone Corporation, appear in the above entitled suit of their own motion and as of right as additional party plaintiffs, and file their bill of complaint herein and are represented by the undersigned as their solicitors and counsel herein.

Dated New York, New York, December 6, 1935.

Allen T. Klots, Hayden N. Smith, Solicitors and Counsel for the Additional Plaintiffs, Office and Post Office Address: No. 32 Liberty Street, Borough of Manhattan, City of New York. Winthrop, Stimson, Putnam & Roberts, Of Counsel.

[fol. 238] IN UNITED STATES DISTRICT COURT

[Title omitted]

BILL OF COMPLAINT OF OHIO ASSOCIATED TELEPHONE COMPANY, INDIANA ASSOCIATED TELEPHONE CORPORATION, MICHIGAN ASSOCIATED TELEPHONE COMPANY, SOUTHWESTERN ASSOCIATED TELEPHONE COMPANY, INTERSTATE TELEPHONE COMPANY, PENNSYLVANIA TELEPHONE CORPORATION AND TRI-STATE ASSOCIATED TELEPHONE CORPORATION, ADDITIONAL PLAINTIFFS—Filed December 6, 1935

To the Honorable Judges of the United States District Court for the Southern District of New York:

Ohio Associated Telephone Company, Indiana Associated Telephone Corporation, Michigan Associated Telephone Company, Southwestern Associated Telephone Company, Interstate Telephone Company, Pennsylvania Telephone Corporation and Tri-State Associated Telephone Corpora-
[fol. 239] tion, as additional parties plaintiff of their own motion and as of right, pursuant to the provisions of the Code of Laws of the United States, Title 28, Section 45 (a), file this, their bill of complaint, against the above named defendants and allege as follows:

1. Ohio Associated Telephone Company now is and at all times hereinafter mentioned was a corporation duly organized and existing under the laws of the State of Ohio, of which state it was and is a citizen and resident with its principal office in the City of Marion, Ohio.

Indiana Associated Telephone Corporation now is and at all times hereinafter mentioned was a corporation duly organized and existing under the laws of the State of Indiana, of which state it was and is a citizen and resident with its principal office in the City of Lafayette, Indiana.

Michigan Associated Telephone Company now is and at all times hereinafter mentioned was a corporation duly organized and existing under the laws of the state of Michigan, of which state it was and is a citizen and resident with its principal office in the City of Muskegon, Michigan.

Southwestern Associated Telephone Company now is and at all times hereinafter mentioned was a corporation duly organized and existing under the laws of the State of

Delaware, of which state it was and is a citizen and resident with an office in the City of Lubbock, Texas.

Interstate Telephone Company now is and at all times hereinafter mentioned was a corporation duly organized and existing under the laws of the State of Idaho, of which state it was and is a citizen and resident with its principal office in the City of Spokane, Washington.

Pennsylvania Telephone Corporation now is and at all times hereinafter mentioned was a corporation duly organized under the laws of the Commonwealth of Pennsyl- [fol. 240] vania, of which commonwealth it was and is a citizen and resident, with an office in the City of Erie, Pennsylvania.

Tri-State Associated Telephone Corporation now is and at all times hereinafter mentioned was a corporation duly organized and existing under the laws of the State of New York of which state it was and is a citizen and resident with an office in the City of Port Jervis, New York.

2. The defendant, Federal Communications Commission (hereinafter referred to as the "Commission"), is an administrative tribunal created by the Communications Act of 1934 and is charged with the administration and enforcement of said Act. The Commission was organized on July 11, 1934, and said Act became effective on that date.

3. Each of said additional plaintiffs (hereinafter referred to as "these plaintiffs") is and at all times since the effective date of said Communications Act has been a carrier engaged in communication for hire in interstate or foreign commerce, subject to the provisions of said Act.

4. The bill of complaint in the above entitled cause was filed by the original plaintiffs in this Court on November 22, 1935, and said cause was commenced in this Court by service of a writ of subpoena and said bill of complaint by filing said subpoena and a copy of the said bill of complaint in the office of the Secretary of said Federal Communications Commission on November 23, 1935, and a subpoena and a copy of said bill of complaint in the Department of Justice on November 23, 1935. The original defendants have not yet filed their answers.

5. Said bill of complaint was brought pursuant to the provisions of the Communications Act of 1934, approved June [fol. 241] 19, 1934 (48 Stat. L. 1064, 1093; Code of Laws of

the United States, Title 47, Section 402 (a)), and of the Urgent Deficiencies Appropriations Act approved October 22, 1913 (38 Stat. L. 219, 220; Code of Laws of the United States, Title 28, Sections 41 (28), 43-48 inclusive), to enjoin, set aside, annul and suspend an order of the Commission, denominated Telephone Division Order No. 7-C dated June 19, 1935, effective January 1, 1936, in proceedings entitled: "In Re: Accounting Rules for Telephone Companies, Interstate Commerce Commission Docket 25705", being docket No. 2551 of the Commission.

6. The interest of these plaintiffs in the above entitled suit arises out of the facts set fort hin paragraphs "2" and "3" above alleged and for the following reasons, to wit:

On August 16, 1934, the Commission issued Telephone Division Order No. 7 notifying state commissions and other parties in interest, including these plaintiffs, that they might file exceptions or objections to a certain report of the Interstate Commerce Commission dated July 9, 1934 in a case identified as "Docket No. 25705, Accounting Rules of Telephone Companies", or suggest amendments to such accounting rules, the case being redocketed and identified as Federal Communications Commission Docket No. 2551. A hearing was thereafter held on November 16, 1934. Thereafter and on May 1, 1935, the Commission issued Telephone Division Order No. 7-B setting forth a proposed Uniform System of Accounts for Telephone Companies entitled "Issue effective January 1, 1936", and therewith a notice to [fol. 242] all parties, including these plaintiffs, that they might file exceptions thereto for consideration by the Commission at a conference with the parties, which was held on May 16, 1935. These plaintiffs duly appeared at said conference and filed exceptions to the proposed Uniform System of Accounts for Telephone Companies.

Thereafter, on June 19, 1935, the Commission issued the order complained of in this suit, designated Telephone Division Order No. 7-C, prescribing, for the use of telephone companies subject to said Act and having average annual operating revenues exceeding $50,000.00, a system of accounts entitled "Uniform System of Accounts for Telephone Companies, Issue of June 19, 1935, Effective January 1, 1936", and requiring every such carrier to keep all accounts in conformity therewith on and after January 1, 1936. A copy of said order No. 7-C, including the text

of said "Issue of June 19, 1935" prescribed thereby, is filed with the original bill of complaint of American Telephone and Telegraph Company, et al., in this cause. Each of these plaintiffs is a telephone company having average annual operating revenues exceeding $50,000.00 and is subject to the provisions of said Order No. 7-C.

7. By reason of the matters hereinabove in paragraph "6" alleged, these plaintiffs are parties in interest to the proceeding before the Commission docketed and identified as Federal Communications Commission Docket No. 2551 in which said Order No. 7-C was made and these plaintiffs appear of their own motion and as of right, as provided in the Code of Laws of the United States, Title 28, Section 45(a) by their solicitors, as parties plaintiff in the above [fol. 243] entitled suit brought by American Telephone and Telegraph Company, et al., wherein the validity of said Order No. 7-C is involved.

8. Said Order No. 7-C is unlawful and void in that it is contrary to Section 404 of said Act and in violation of the rights of these plaintiffs under the due process clause of the Fifth Amendment to the Constitution of the United States, for the reason that in said proceeding and investigation the Commission made no report in writing, no findings and no statement of its conclusions.

9. Said Order and the Uniform System of Accounts prescribed thereby require that these plaintiffs set up in their books of account Account No. 100.1 known as "Telephone Plant in Service" and that in this account these plaintiffs' properties used in telephone service shall be carried at their original cost. This original cost is defined by Instructions 3-S.1 of said Uniform System of Accounts as

"the actual money cost of (or the current money value of any consideration other than money exchanged for) property at the time when it was first dedicated to the public use, whether by the accounting company or by a predecessor public utility."

They then proceed to require in substance that in an Account No. 100.4 known as "Telephone Plant Acquisition Adjustment" there shall be carried the difference between the amount of money actually paid by these plaintiffs for

the companies' properties used in telephone service and the original cost thereof as carried in Account No. 100.1 above described.

They then further require that these plaintiffs shall record nothing in their accounts on account of the expense [fol. 244] of depreciation with respect to the portion of their property investment which is to be recorded in Account No. 100.4 "Telephone Plant Acquisition Adjustment."

They then further provide that the amounts recorded in said "Telephone Plant Acquisition Adjustment" account with respect to each property acquisition "shall be disposed of, written off, or provisions shall be made for the amortization thereof in such manner as this Commission may direct." (100.4(C)).

The greater part of these plaintiff's properties was acquired by them from other public utility companies and in many cases these companies had acquired such properties from still other public utility companies. The greater part of such property which is now in existence has been recorded in these plaintiffs' property investment accounts at its actual cost to these plaintiffs either in cash or securities. Such property is of substantial value.

The requirements above stated of said Order and said "Uniform System of Accounts" are arbitrary, unreasonable are beyond the statutory power and authority of the Commission, constitute an abuse of that power and authority and an attempt to deprive these plaintiffs of their property without due process of law in violation of the Fifth Amendment to the Constitution of the United States and are illegal and void for the following reasons:

a. The purpose of an account, according to legitimate and correct accounting practice, and of a balance sheet based upon such an account, is truly to reflect the actual financial transactions and condition of the accounting company. The maintenance of such an accurate record of financial facts is essential from the point of view of all persons interested in the company, including bondholders, [fol. 245] stockholders, directors and officers of the company, the investing public, ratepayers, as well as regulating commissions and taxing authorities. When a company purchases property for use in its business the essential fact to be recorded as an indispensable item of its financial his-

tory is the cost to that company of the property acquired and not the cost of that property to some one else. The maintenance of the integrity of that item of actual cost is vital if the account is to be a true record of the financial facts relating to that company. The requirements that there shall be segregated a part of this actual cost to the accounting company in a separate account which the Commission by this Order proposes to treat in a separate and independent manner violates in an essential and vital respect the integrity of such an account. That it is the purpose of the Commission in requiring the segregation of these plaintiffs' actual costs into two accounts to treat in a separate and independent manner the different portions thereof, is shown first by the very denomination of Account No. 100.4 as "Telephone Plant Acquisition Adjustment" Account, second, by the provisions of Section 100.4(C) to the effect that the amounts recorded in said account "shall be disposed of, written off or provisions shall be made for the amortization thereof in such manner as this Commission may direct", and third, by the failure of the Order to provide for charges to depreciation with respect to the amounts carried in said Account No. 100.4.

b. The requirement that a portion of these plaintiffs' actual costs of property used in their business shall be carried in said Plant Acquisition Adjustment Account and that the items in such account shall be disposed of, written off or provisions shall be made for the amortization thereof [fol. 246] in such manner as the Commission may direct, immediately and forthwith reduces, if not destroys, the value of items included in said account as physical assets on these plaintiffs' balance sheets. The power thus assumed by the Commission to dispose of these items in any manner which it sees fit immediately arouses suspicion as to the substantial character of the items in the account. Furthermore, the arbitrary segregation of these plaintiffs' actual costs into separate accounts as aforesaid results in giving the entirely false and erroneous impression that the portion of the cost to these plaintiffs included in Account No. 100.4, namely, the "Telephone Plant Acquisition Adjustment" account, is not the true cost, but an inflated or intangible value, which is entirely contrary to fact.

c. The real purpose of requiring this division of the actual cost of the plant into two accounts and the setting

up of the Telephone Plant Acquisition Adjustment Account, No. 100.4, appears from an analysis of the provisions of said Order and said Uniform System of Accounts in their entirety. Such an analysis will disclose that the establishment of this account is only preparatory to a requirement that the items placed therein shall be written off or amortized or in some other manner eliminated from the assets of the company. The actual cost to these plaintiffs representing their actual investment in their properties has not only in most cases been approved by a governmental commission at the time of acquisition, but has been used in the companies' accounts as a basis for their financial operations, including the issuance of securities and otherwise. This Commission has no right, either as an incident to its power [fol. 247] to prescribe uniform systems of accounting or otherwise under the Act, to require these plaintiffs to write off in this manner a portion of their actual investment or otherwise to dispose of it as the Commission may direct. No principle is prescribed by the statute upon which the ultimate disposition by the Commission can be made and no standard is set up by which its action is to be guided. To require a classification of accounts which is solely directed to this unauthorized and illegal end, is unauthorized, unreasonable and arbitrary.

d. In so far as any legitimate purpose can be gained by requiring information as to the original cost of plant acquired, the same can be achieved by requiring from these plaintiffs a statement contemplated by, and provided for in, Section 213(c) of the Act. This section provides in part as follows:

"The Commission may at any time require any such carrier to file with the Commission a statement showing the original cost at the time of dedication to the public use of all or of any part of the property owned or used by said carrier. For the showing of such original cost said property shall be classified, and the original cost shall be defined, in such manner as the Commission may prescribe; and if any part of such cost cannot be determined from accounting or other records, the portion of the property for which such cost cannot be determined shall be reported to the Commission; and, if the Commission shall so direct, the original cost thereof shall be estimated in such manner as the Commission may prescribe. * * *"

In fact, the inclusion of Section 213(c) in said Act indicates that the statute contemplates that whatever information the Commission desires in respect to original cost is to be procured by means of such a statement which can be furnished without violating the integrity of the companies' accounts. The properties of these plaintiffs, for example, are com- [fol. 248] posed for the most part of a large number of very small properties in rural communities previously owned by small local companies. Because of the inaccuracy or incompleteness of the records kept by the preceding owners of these properties, it will be impossible for these plaintiffs accurately to ascertain the actual money cost of these at the time when they were first dedicated to the public use. The determination of such original cost will thus necessarily be a matter of estimate and conjecture and cannot be made with any degree of accuracy. To inject such items in the balance sheets and account books of the companies will result in a misleading and inaccurate picture of these plaintiffs' true financial condition and history, whereas every legitimate purpose can be served by confining such figures of original cost to the statement provided for in Section 213(c), as aforesaid. In view of the foregoing, said requirement that these figures shall be injected in the balance sheets and account books of the companies is arbitrary and unreasonable.

e. The requirements aforesaid prevent these plaintiffs from recording in their expense accounts the expense of depreciation which they actually incur.

f. Said requirements are impracticable of application in these plaintiffs' accounting. They would necessitate establishing the identity of items of purchased property many years after the purchase, when many of the purchased items had been retired and when the surviving items had become so commingled with previously owned and subsequently constructed plant that their identification would be impossible. They would necessitate the separation into two accounts of the investment of these plaintiffs in a single item of purchased property, and when it became necessary to [fol. 249] write it out of the accounts upon the retirement of that item, there would be no practical way of distinguishing items which had been charged to the two accounts from commingled nonpurchased items of the same kind which had been charged to only one account. These difficulties

would add greatly to the accounting expense of these plaintiffs and would result in their accounts reflecting, in part, unreliable estimates instead of facts.

g. Said requirements compel these plaintiffs to make radical changes in their completed accounts The Communications Act does not empower the Commission to prescribe retroactive changes in accounts which have been lawfully and correctly kept, but only to prescribe the forms of accounts, records and memoranda to be kept in the future.

h. They require the amounts recorded in Account 100.4, "Telephone Plant Acquisition Adjustment", to be disposed of, written off or amortized by these plaintiffs, not in accordance with any accounting rule or classification prescribed by the Commission as a part of said system of accounts or otherwise, but in such manner as the Commission may direct as to each individual property acquisition. The Commission's authority is limited to the making of rules, regulations and classifications, in accordance with which all carriers within a class must keep their accounts or suffer the penalties prescribed by the Act. It has no authority to issue an individual order requiring an individual carrier to make such specific accounting entry as it may direct with respect to a transaction as to which it has made no accounting rules, regulations or classifications.

i. Said requirements are inconsistent with and contrary to Sections 213(c) and 219(a) of said Act, and in violation [fol. 250] of Section 4(i) thereof, and bear no reasonable relationship to the ends and purposes for which the Commission is authorized by said Act to prescribe the forms of accounts to be kept by carriers subject thereto.

10. Said Order and "Uniform System of Accounts" prescribed thereby requires that where these plaintiffs purchase from another public utility, property which was donated to such public utility, these plaintiffs shall record as a liability, in an account entitled "Contributions of Telephone Plant", the amount of the donation to the prior owner. To thus require these plaintiffs' accounts to show a liability for a contribution which these plaintiffs have not received is arbitrary and unreasonable, beyond the statutory power and authority of the Commission and therefore illegal and void.

11. Said Order and "Uniform System of Accounts" requires these plaintiffs to include a part of their investment in property in Account 100.1, "Telephone Plant in Service", a part in Account 100.3, "Property Held for Future Telephone Use" and a part in Account 103, "Miscellaneous Physical Property." The dividing lines between these classifications, as stated in said system of accounts, are so indefinite and ambiguous that it will be impossible for these plaintiffs to know to which account substantial amounts of their property should be charged. These plaintiffs will of necessity be required to make entries in these accounts at their peril, at the risk of the penalties prescribed by said Act. The Commission is without authority to prescribe such classifications and the exaction of obedience to rules so vague and indefinite is in violation of the rights of these plaintiffs under the Fifth and Sixth Amendments to the [fol. 25] Constitution of the United States, which require due process of law and that persons accused of crime shall be adequately informed of the nature and cause of the accusation.

12. The nature of these plaintiffs' business is such that a portion of their property during periods of its life necessarily constitutes what is known as spare plant. Said Order and "Uniform System of Accounts" requires that such property be included in Account 100.3, "Property Held for Future Telephone Use", during such periods. Said system also requires the computation of depreciation expense at rates based on the entire life of the property, including the portion of its life during which it is included in Account 100.3, but prevents the recording of any depreciation expense with respect to such property during the period in which it is included in Account 100.3. The result is that these plaintiffs will be prevented from recording on their books the full expense of depreciation with respect to property which, during any portion of its life, is included in Account 100.3, "Property Held for Future Telephone Use." The said requirements are contrary to the fundamental principles of correct accounting, arbitrary, unreasonable and confiscatory, and are therefore illegal and void.

13. Said Order and "Uniform System of Accounts" requires that all charges to plant investment, income, operat-

ing revenue and operating expense accounts shall be just and reasonable and that any payments by these plaintiffs in excess of such just and reasonable charges shall be charged against income. This requirement is contrary to the fundamental principles of correct accounting, arbitrary and unreasonable, in that it will require the accounts to record judgment as to what should have been spent, instead of the fact of what was spent, and for the further [fol. 252] reason that the words "just and reasonable" in their context are vague, lacking in precise definition and susceptible of a wide variation of opinion, so that it will be impossible for these plaintiffs to know to what account their expenditures should be charged. These plaintiffs will of necessity be required to make all charges to these accounts at their peril, at the risk of the penalties prescribed by said Act. The Commission is without authority to prescribe such a requirement and the exaction of obedience to a rule so vague and indefinite is in violation of the rights of these plaintiffs under the Fifth and Sixth Amendments to the Constitution of the United States, which require due process of law and that persons accused of crime shall be adequately informed of the nature and cause of the accusation.

14. These plaintiffs have for many years filed with governmental agencies and issued to investors and to the public financial statements taken from their books of account as heretofore kept, and said books of account have formed the basis of their corporate financing and of many other matters affecting their very existence. The Order and "Uniform System of Accounts" complained of would result in the publication of financial statements radically different from those heretofore issued. The enforced publication of statements which would contradict those on which these plaintiffs' entire financial structures have been based would seriously impair these plaintiffs' credit, and thus take their property without due process of law in violation of the Fifth Amendment to the Constitution of the United States.

15. Said "Issue of June 19, 1935," purports to constitute a complete system of accounts; its provisions are inter- [fol. 253] dependent and nonseverable, and it is impossible practically and legally to separate the provisions which affectuate the illegal requirements hereinabove set forth

from the other provisions thereof. Said "Issue of June 19, 1935", and said Order No. 7-C prescribing the same, are therefore illegal and void in their entirety, upon all the grounds hereinabove alleged.

16. Said Order No. 7-C requires these plaintiffs, during the year 1936, to keep not only the complete system of accounts prescribed thereby, but also such portion or portions of their present accounts as may be necessary for comparison of 1936 results with results of previous years. The changes in these plaintiffs' accounting required by said Order No. 7-C affect so many of these plaintiffs' present accounts that compliance with the above requirement would compel plaintiffs, at great expense, to keep almost a complete set of accounts in accordance with the present system in addition to a complete set of accounts in accordance with the system prescribed by said order. The said requirement is arbitrary and unreasonable, beyond the statutory power and authority of the Commission, and therefore illegal and void.

17. Said Order and "Uniform System of Accounts" unlawfully prevents each of these plaintiffs herein from capitalizing in its books of account the full actual cost of organizing its business. Instruction 20 entitled "Purpose of Telephone Plant Accounts" states that it shall include the general expenses of organization of the accounting company. This is set up in Account 201, "Organization", and is a part of the Balance Sheet Account 100.1, "Telephone Plant in Service."

[fol. 254] There is not included, however, in the items classified under Account 201, certain legitimate organization expenses incurred in connection with the issuance and sale of capital stock. According to said Uniform System of Accounts these are to be included in Account 134.2, known as, "Capital Stock Expense", under the heading "Prepaid Accounts and Deferred Charges", and the regulations require in 134.2(c) that the only way the company may amortize or write off the balance carried in this account is by credit to surplus and cannot, therefore, amortize it through operating expense.

These plaintiffs are lawfully entitled either to receive a return on this investment which is a legitimate organization expense, or to amortize such investment through operating expense.

The said requirement is contrary to establish accounting practice, deprives each plaintiff of its lawfully acquired corporate assets, confiscates its property and is beyond the statutory powers of the Commission.

18. Said Order and "Uniform System of Accounts" establishes a separate expense account for the maintenance [fol. 255] expenses of each class of plant. Whereas the Uniform System of Accounts in effect until January 1, 1936 provides one account, Repairs of Outside Plant, the Uniform System of Accounts effective January 1, 1936 will provide nine accounts as follows:

602.1. Repairs of pole lines.
602.2. Repairs of aerial cable.
602.3. Repairs of underground cable.
602.4. Repairs of buried cable.
602.5. Repairs of submarine cable.
602.6. Repairs of aerial wire.
602.7. Repairs of underground conduit.
602.8. Shop repairs and salvage adjustments.
602.9. General supervision, engineering, and tool expenses.

As heretofore alleged, these plaintiffs are composed primarily of many small exchanges. Maintenance work in most cases is performed by individuals or small groups without foremen or timekeepers. It is impossible from a practical standpoint for these plaintiffs' repairmen accurately to record the amount of time spent and materials used on the nine Repair accounts.

Such a requirement is arbitrary, unjust, unreasonable and places an added burden on these plaintiffs unjustified by any end sought to be gained and is contrary to law.

19. In the premises, these plaintiffs have no adequate remedy at law, and unless the relief prayed for herein be granted to these plaintiffs, they will suffer, for the reasons and in the manner stated in this bill of complaint, irre- [fol. 256] parable injury and damage.

20. These plaintiffs are advised and therefore allege that unless said order of the Commission and said system of accounts prescribed thereby are complied with on and after January 1, 1936, or unless prior to that date these plaintiffs are afforded the protection, by a writ of injunction, which

this court alone is competent to grant, they and their officers and employees will, under the terms of the Communications Act of 1934, and particularly under Sections 220, 501 and 502 thereof, be subjected to a multiplicity of suits and criminal prosecutions for the recovery and assessment of the fines and penalties in said sections provided. If said order and said system of accounts prescribed thereby are enjoined, set aside, annulled and suspended as hereinafter prayed, these plaintiffs will be required to continue keeping all their accounts, records and memoranda in accordance with the system of accounts entitled "Uniform System of Accounts for Telephone Companies, First Revised Issue", prescribed by an order of the Interstate Commerce Commission dated November 12, 1932, effective January 1, 1933, which is still in full force and effect and which will remain in full force and effect by virtue of Section 604(a) of said Communications Act until rescinded or superseded by a valid order of the Federal Communications Commission.

21. These plaintiffs are further advised by counsel and are informed and believe and therefore allege that this is a case of actual controversy, involving property belonging to these plaintiffs in which this Court, pursuant to Section [fol. 257] 274(d) of the Judicial Code, Title 28, Section 400 U. S. C. A., has the power to declare rights and other legal relations and that these plaintiffs are interested parties petitioning for such declaration.

Wherefore, these plaintiffs pray:

1. That a subpœna or subpœnas in chancery issue out of or under the seal of this Honorable Court directed to the defendants as required by law, and that due and proper service of such process and of this bill of complaint be forthwith made by filing a copy thereof in the office of the Secretary of the Commission and another copy in the Department of Justice as in said Urgent Deficiencies Appropriations Act provided, and that thereby the defendants and each of them be required on or before a date to be specified in such subpœna or notice, to appear herein and answer this bill of complaint, but not under oath, answer under oath being expressly waived.

2. That the court, as soon as practicable, convene a specially constituted court of three judges, as required by

Title 28, Section 47, Code of Laws of the United States; and that a temporary or interlocutory injunction be entered herein, restraining, enjoining and suspending, until the further order of this court, the operation, execution, effect and enforcement of said order of the Commission.

3. That pending a hearing upon the aforesaid application for a temporary or interlocutory injunction a preliminary restraining order be issued in term restraining, enjoining and suspending the operation, execution, effect and enforcement of said order of the Commission until said application [fol. 258] for a temporary or interlocutory injunction shall have been heard and determined.

4. That after final hearing this court adjudge, order and decree that said order of the Commission is and has at all times been beyond the lawful authority of the Commission, in violation of the legal rights of these plaintiffs, and wholly void; and that said order be perpetually vacated, set aside, suspended, and annulled, and the enforcement thereof perpetually restrained and enjoined.

5. That said Order and said Uniform System of Accounts issued pursuant thereto and the whole thereof be declared and determined by this court to be beyond the lawful authority of the Commission, in violation of the legal rights of these plaintiffs, and wholly void.

6. That these plaintiffs may have such other and further relief in the premises as to equity and justice may appertain and as may be deemed by this Honorable Court to be adequate and proper under the circumstances.

Allen T. Klots, Hayden N. Smith, Solicitors and counsel for additional plaintiffs Ohio Associated Telephone Company, Indiana Associated Telephone Corporation, Michigan Associated Telephone Company, Southwestern Associated Telephone Company, Interstate Telephone Company, Pennsylvania Telephone Corporation and Tri-State Associated Telephone Corporation, Office and Post Office Address, No. 32 Liberty Street, New York, N. Y. Winthrop, Stimson, Putnam & Roberts, of Counsel.

[fols. 259-265] *Duly sworn to by Harry M. Eugh et al. Jurats omitted in printing.*

[fol. 266] IN UNITED STATES DISTRICT COURT

[Title omitted]

ORDER APPROVING ADDITIONAL PLAINTIFFS APPEARANCE, ETC.—
Filed December 10, 1935

Ohio Associated Telephone Company, Indiana Associated Telephone Corporation, Michigan Associated Telephone Company, Southwestern Associated Telephone Company, Interstate Telephone Company, Pennsylvania Telephone Corporation, Tri-State Associated Telephone Corporation.

The above-named Additional Plaintiffs, having this day filed their verified bill of complaint herein, pursuant to the [fol. 267] provisions of the Code of Laws of the United States, Title 28, Section 45 (a), and having this day moved the Court upon said bill of complaint and the affidavit of Harold V. Bozell, sworn to on the 6th day of December, 1935, for an order upon the defendants to show cause, if any they have, why the Court should not grant their application for an interlocutory injunction suspending during the pendency of said cause the operation of that certain order of the Federal Communications Commission designated "Telephone Division Order No. 7-C," dated June 19, 1935, effective January 1, 1936, prescribing a Uniform System of Accounts for Telephone Companies, and for a temporary stay of the operation of said order pending the determination of said application for an interlocutory injunction, all in accordance with the provisions set forth in their said bill of complaint and said affidavit, it is

Ordered, that said Ohio Associated Telephone Company, Indiana Associated Telephone Corporation, Michigan Associated Telephone Company, Southwestern Associated Telephone Company, Interstate Telephone Company, Pennsylvania Telephone Corporation and Tri-State Associated Telephone Corporation be and they hereby are authorized and permitted to appear herein as additional parties plaintiff to this cause; and it is further

Ordered, that the defendants herein, the United States of America and the Federal Communications Commission, appear before the undersigned and the Honorable Martin T.

Manton and the Honorable A. N. Hand, Circuit Judges, the Court constituted in accordance with the provisions of Title 28, Section 47, Code of Laws of the United States, on the 13th day of December, 1935, at 2:30 o'clock in the after- [fol. 268] noon of that day in Room 433 in the Post Office Building, Park Row and Broadway, in the Borough of Manhattan, City, County and State of New York, and then and there show cause before the Court why the interlocutory injunction and the temporary stay so prayed for in said bill of complaint and in said motion should not be issued; and it is further

Ordered, that a copy of this order to show cause and of the said motion and affidavit be served upon the Attorney General of the United States of America and upon the Secretary or Chief Counsel of the Federal Communications Commission on or before the 7th day of December, 1935; and it is further

Ordered, that the defendants shall serve upon the solicitors or counsel for these Additional Plaintiffs, on or before December 12, 1935, copies of such affidavits, if any, as may be offered at said hearing in opposition to said motion.

(Signed) Jno. C. Knox, U. S. D. J.

Dated New York, New York, December 6, 1935.

[fol. 269] In United States District Court

[Title omitted]

Order to Show Cause—Filed December 12, 1935

[fol. 270] Plaintiffs having this day moved the court, upon their verified bill of complaint heretofore duly filed herein, and the affidavits of Andrew Sangster, sworn to the 5th day of December, 1935, and of John T. Madden, Roy B. Kester, B. F. Young and Charles A. Heiss, sworn to the 6th day of December, 1935, for an order upon the defendants to show cause, if any they have, why the court should not grant their application for an interlocutory injunction suspending, during the pendency of said cause, the operation of that certain order of the Federal Communications Commission designated "Telephone Division Order No. 7-C", dated June 19, 1935, effective January 1, 1936, prescribing a Uni-

form System of Accounts for Telephone Companies, and for a temporary stay of the operation of said order pending the determination of said application for an interlocutory injunction, all in accordance with the prayers set forth in their said bill of complaint.

It is ordered that the defendants herein, United States of America and the Federal Communications Commission, appear before the undersigned, and the Honorable Martin T. Manton and the Honorable A. N. Hand, Circuit Judges, the court constituted in accordance with the provisions of Title 28, Section 47, Code of Laws of the United States, on the 13th day of December, 1935, at 2:30 o'clock in the afternoon of that day in Room 433 in the Post Office Building, Park Row and Broadway, in the Borough of Manhattan, City, County and State of New York, and then and there show cause before the court why the interlocutory injunction and the temporary stay so prayed for in said bill of complaint and in said motion should not be issued;

[fol. 271] It is further ordered that a copy of this order to show cause and of the said motion and affidavits be served upon the Attorney General of the United States of America and upon the Secretary or Chief Counsel of the Federal Communications Commission on or before the 7th day of December, 1935;

It is further ordered that the defendants shall serve upon the solicitors for plaintiffs, or one of the solicitors, on or before December 12, 1935, copies of such affidavits, if any, as may be offered at said hearing in opposition to said motion.

Jno. C. Knox, United States District Judge.

Dated, New York, N. Y., this 6th day of December, 1935.

[fol. 272] IN UNITED STATES DISTRICT COURT

[Title omitted]

RESPONSE OF FEDERAL COMMUNICATIONS COMMISSION TO ORDER TO SHOW CAUSE—Filed December 12, 1935

The Federal Communications Commission, hereinafter called the Commission, party defendant in the above-entitled suit, now comes and answers so much of the order to

show cause of this Honorable Court dated December 6, 1935, as requires this defendant to serve upon the solicitors for plaintiffs, or one of the solicitors, on or before December 12, 1935, copies of such affidavits, if any, as may be offered at said hearing in opposition to said motion, respectfully represents:

(1) That there is annexed hereto the affidavits of William J. Norfleet, Robert S. Rains, John H. Bickley, Asel R. Colbert, Malcolm F. Orton, and Charles W. Smith, all sworn to the 11th day of December, 1935.

(2) Copies of such affidavits have been served upon C. M. Bracelen, 195 Broadway, New York, New York, solicitor for plaintiffs, American Telephone and Telegraph Company, et al., and Eastern Telephone and Telegraph Company, et al., [fol. 273] additional plaintiffs; and upon Allen T. Klots, 32 Liberty Street, New York, New York, solicitor for Ohio Associated Telephone Company, et al., additional plaintiffs.

Federal Communications Commission, by Albert E. Stephan, W. D. Humphrey, Hampson Gary, General Counsel; Frank Roberson, Assistant General Counsel, of Counsel.

[fol. 274] IN UNITED STATES DISTRICT COURT

[Title omitted]

NOTICE OF PETITION FOR LEAVE TO INTERVENE—Filed December 16, 1935

Please Take Notice that the undersigned will appear before this Court on the 13th day of December, 1935, at 2:30 o'clock in the afternoon of that day, or as soon thereafter as counsel can be heard, in Room 433 in the Post Office Building, Park Row and Broadway, in the Borough of Manhattan, City, County and State of New York, and will then and there move the said court for an order granting leave to Eastern Telephone and Telegraph Company, Moosehead Telephone and Telegraph Company, Nicollet County Telephone and Telegraph Company, Rio Grande Valley Tele- [fol. 275] phone Company, The Crown Point Telephone Company, The Emporia Telephone Company, Westerly Au-

tomatic Telephone Company and Western New England Telephone Company to intervene in the above-entitled cause and to be made intervening plaintiffs therein, with leave to file their bill of intervention therein, to be represented by counsel, and generally to prosecute said cause as intervening plaintiffs, in accordance with their Petition for Leave to Intervene, hereto attached; and if such leave be granted, will move in open court at said hearing for an interlocutory injunction suspending, during the pendency of said cause, the operation of that certain order of the Federal Communications Commission designated "Telephone Division Order No. 7C", dated June 19, 1935, effective January 1, 1936, and for a temporary stay of the operation of said order to be in effect pending the determination of said application for an interlocutory injunction, upon the grounds and in the manner set forth in the bill of intervention, copy of which is attached to said petition for leave to intervene.

Dated at New York, New York, this 10th day of December, 1935.

C. M. Bracelen, Chas. T. Russell, Alan J. McBean, Solicitors for Petitioners, Address: 195 Broadway, New York, New York.

[fol. 276] To the Attorney-General of the United States, General Counsel of the Federal Communications Commission, Allen T. Klotz, Esq.

[fol. 277] IN UNITED STATES DISTRICT COURT

[Title omitted]

PETITION FOR LEAVE TO INTERVENE—Filed December 16, 1935

Come now Eastern Telephone and Telegraph Company, Moosehead Telephone and Telegraph Company, Nicollet County Telephone and Telegraph Company, Rio Grande Valley Telephone Company, The Crown Point Telephone Company, The Emporia Telephone Company, Westerly Automatic Telephone Company and Western New England Telephone Company by the undersigned, their solicitors, and file this their petition for leave to intervene in the above entitled cause, and respectfully allege and show as follows:

1. Each of said petitioners above mentioned now is and at all times hereinafter mentioned was a corporation duly

[fol. 278] organized and existing under the laws of one of the States of the United States, the State of incorporation, date of incorporation, and the address of the principal office of each being as follows:

Eastern Telephone and Telegraph Company, Maine, July 27, 1911, Calais, Maine.

Moosehead Telephone and Telegraph Company, Maine, May 15, 1915, Dover-Foxcroft, Maine.

Nicollet County Telephone and Telegraph Company, Minnesota, April 23, 1898, St. Paul, Minnesota.

Rio Grande Valley Telephone Company, Texas, June 6, 1923, McAllen, Texas.

The Crown Point Telephone Company, Indiana, April 6, 1896, Crown Point, Indiana.

The Emporia Telephone Company, Kansas, June 14, 1901, Emporia, Kansas.

Westerly Automatic Telephone Company, Rhode Island, April 21, 1902, Westerly, Rhode Island.

Western New England Telephone Company, Massachusetts, February 14, 1898, Shelburne Falls, Massachusetts.

2. The bill of complaint in the above entitled cause was filed in this court on November 22, 1935, and said cause was commenced in this court by the service of a writ of subpœna and said bill of complaint by filing a copy of said subpœna and a copy of said bill of complaint in the office [fol. 279] of the Secretary of the Federal Communications Commission (hereinafter referred to as the Commission) on November 23, 1935, and a copy of said subpœna and a copy of said bill of complaint in the Department of Justice on November 23, 1935. Defendants have not yet filed their answers to said bill of complaint.

3. Said bill of complaint was brought pursuant to the provisions of the Communications Act of 1934, approved June 19, 1934 (48 Stat. L. 1064, 1093; Code of Laws of the United States, Title 47, Section 402 (a)), and of the Urgent Deficiencies Appropriations Act approved October 22, 1913 (38 Stat. L. 219, 220; Code of Laws of the United States, Title 28, Sections 41 (28), 43-48, inclusive), to enjoin, set aside, annul and suspend an order of the Commission designated "Telephone Division Order No. 7-C" prescribing for the use of Telephone Companies subject to the Communica-

tions Act and having average annual operating revenues exceeding $50,000 a system of accounts entitled "Uniform System of Accounts for Telephone Companies, Issue of June 19, 1935, Effective January 1, 1936," and requiring every such carrier to keep all accounts in conformity therewith on and after January 1, 1936; said Bill of Complaint further praying for an interlocutory injunction suspending during the pendency of said cause the operation of said order and for a temporary stay of the operation of said order to be in effect pending the determination of said ap- [fol. 280] plication for an interlocutory injunction.

4. The plaintiffs herein, on the 6th day of December, 1935, moved this court for an order to show cause why their application for such interlocutory injunction and such temporary stay should not be granted; and this court, pursuant to said motion, ordered the defendants herein, to appear before the Honorable Martin T. Manton and Honorable A. N. Hand, Circuit Judges, and the Honorable John C. Knox, District Judge, a court constituted in accordance with the provisions of Title 28, Section 47, Code of Laws of the United States, on the 13th day of December, 1935, at 2:30 o'clock in the afternoon of that day, in Room 433 in the Post Office Building, Park Row and Broadway, in the Borough of Manhattan, City, County and State of New York, and then and there show cause before said court why the interlocutory injunction and the temporary stay so prayed for in the plaintiffs' bill of complaint and in said motion should not be issued.

5. Each of said petitioners is now and at all times since the effective date of the Communications Act of 1934, approved June 19, 1934, (48 Stat. L. 1064, 1093, Code of Laws of the United States, Title 47, Section 402 (a)), has been a carrier engaged in communication for hire in interstate [fol. 281] or foreign commerce, subject to the provisions of said Act.

6. Each of said petitioners is a telephone company having average annual operating revenues exceeding $50,000, and is a carrier subject to the order of the Commission designated "Telephone Division Order No. 7-C" hereinabove referred to in Section 3. Said order is in violation of the legal rights of each of said petitioners, as more particularly alleged in petitioners' proposed Bill of Interven-

tion, a copy of which is attached hereto and made a part hereof.

7. Each of said petitioners has an interest in the litigation of the above entitled cause against the defendants therein, as shown by the facts hereinabove alleged and the facts alleged in the petitioners' proposed Bill of Intervention; and petitioners cannot adequately protect their rights and interests unless permitted to intervene in said cause as herein prayed, and unless said rights and interests are protected your petitioners will suffer grave and irreparable damage and injury.

8. Wherefore, said petitioners and each of them respectfully pray that the Court enter an order permitting each of them to intervene in the above entitled cause and making each of them an Intervening Plaintiff therein, with the right to file the attached proposed Bill of Intervention within a [fol. 282] time to be set by the Court, to be represented by counsel, and generally to prosecute said cause as an Intervening Plaintiff therein, all in accordance with Title 28, Section 45 (a), Code of Laws of the United States, and for such other and further relief as may be proper in the premises.

(Sgd.) C. M. Bracelen, Chas. T. Russell, Alan J. McBean, Solicitors for Petitioners, Address: 195 Broadway, New York, New York.

[fol. 283] IN UNITED STATES DISTRICT COURT

[Title omitted]

ORDER GRANTING LEAVE TO INTERVENE—Filed December 16, 1935

On this 13th day of December, 1935, the petition of Eastern Telephone and Telegraph Company, Moosehead Telephone and Telegraph Company, Nicollet County Telephone and Telegraph Company, Rio Grande Valley Telephone Company, The Crown Point Telephone Company, The Emporia Telephone Company, Westerly Automatic Telephone [fol. 284] Company and Western New England Telephone Company for leave to intervene in this cause as intervening plaintiffs came on to be heard, and the said Petition for Leave to Intervene and intervening plaintiffs' proposed

Bill of Intervention thereunto annexed having been duly considered, and it appearing to the court that said petitioners are carriers engaged in communication for hire in interstate or foreign commerce, subject to the provisions of the Communications Act of 1934, and are subject to, and required to comply with, the provisions of a certain order of the Federal Communications Commission, designated "Telephone Division Order No. 7-C," establishing a Uniform System of Accounts for Telephone Companies, effective January 1, 1936, as more particularly described in said Petition for Leave to Intervene and in said Bill of Intervention.

It is Hereby Ordered by the court that the said petitioners, and each of them, be and they hereby are granted leave to intervene in the above-entitled cause, and they are hereby made intervening plaintiffs therein; that leave is hereby granted said petitioners to file therein their Bill of Intervention, in conformity with the proposed Bill appended to [fol. 285] their said Petition, and to be represented by counsel, and generally to prosecute said cause as plaintiffs therein.

It is Further Ordered that the service of the subpœna herein and the said Bill of Intervention may be made by S. Whitney Landon, Esq., an attorney in the office of the American Telephone and Telegraph Company, one of the plaintiffs herein, and he is hereby appointed by this Court for said purpose in accordance with Equity Rule No. 15.

Jno. C. Knox, United States District Judge.

[fol. 286] In United States District Court

[Title omitted]

Bill of Intervention of Eastern Telephone and Telegraph Company, Moosehead Telephone and Telegraph Company, Nicollet County Telephone and Telegaph Company, Rio Grande Valley Telephone Company, The Crown Point Telephone Company, The Emporia Telephone Company, Westerly Ahtomatic Telephone Company, and Western New England Telephone Company, Intervening Plaintiffs—Filed December 14, 1935

To the Honorable the Judges of Said District Court:

Come now the above named intervening plaintiffs and by leave of Court first obtained, file this their bill of inter-

vention herein, pursuant to the provisions of the Communications Act of 1934, approved June 19, 1934, (48 Stat. L. 1064, 1093; Code of Laws of the United States, Title 47, Section 402 (a)), and of the Urgent Deficiencies Appropria-
[fol. 287] tions Act, approved October 22, 1913 (38 Stat. L. 219, 220; Code of Laws of the United States, Title 28, Secs. 41 (28), 43-48, inclusive), to enjoin, set aside, annul and suspend an order of the Federal Communications Commission (hereinafter referred to as the Commission) denominated Telephone Division Order No. 7-C, dated June 19, 1935, effective January 1, 1936, in proceedings entitled:

"In re: Accounting Rules for Telephone Companies, Interstate Commerce Commission Docket No. 25705,"

being Docket No. 2551 of the Commission.

For their cause of action intervening plaintiffs allege:

1. Each of said intervening plaintiffs above mentioned now is and at all times hereinafter mentioned was a corporation duly organized and existing under the laws of one of the states of the United States, the state of incorporation, date of incorporation, and the address of the principal office of each being as follows:

Eastern Telephone and Telegraph Company, Maine, July 27, 1911, Calais, Maine.

Moosehead Telephone and Telegraph Company, Maine, May 15, 1915, Dover-Foxcroft, Maine.

Nicollet County Telephone and Telegraph Company, Minnesota, April 23, 1898, St. Paul, Minnesota.

Rio Grande Valley Telephone Company, Texas, June 6, 1923, McAllen, Texas.

[fol. 288] The Crown Point Telephone Company, Indiana, April 6, 1896, Crown Point, Indiana.

The Emporia Telephone Company, Kansas, June 14, 1901, Emporia, Kansas.

Westerly Automatic Telephone Company, Rhode Island, April 21, 1902, Westerly, Rhode Island.

Western New England Telephone Company, Massachusetts, February 14, 1898, Shelburne Falls, Massachusetts.

2. The Commission is an administrative tribunal created by the Communications Act of 1934, and is charged with the administration and enforcement of said Act. The Com-

mission was organized on July 11, 1934, and said Act became effective on that date.

3. Each of said intervening plaintiffs is and at all times since the effective date of said Communications Act has been been a carrier engaged in communication for hire in interstate or foreign commerce, subject to the provisions of said Act.

4. Before and until the enactment of the Communications Act each of said intervening plaintiffs was a common carrier engaged in the transmission of intelligence for hire in interstate commerce and was subject to the jurisdiction of the Interstate Commerce Commission under the provisions of the Interstate Commerce Act as amended.

[fol. 289] The Interstate Commerce Commission, pursuant to the authority vested in it as aforesaid, entered an order date November 12, 1932, prescribing for certain telephone companies, including each of said intervening plaintiffs, a uniform system of accounts entitled "Uniform System of Accounts for Telephone Companies, First Revised Issue," effective January 1, 1933.

Compliance with said order was obligatory upon each of the intervening plaintiffs at all times subsequent to the effective date thereof, and compliance therewith is now obligatory upon all of them, and intervening plaintiffs are prohibited by law from keeping any other or different accounts than those so prescribed. At all times subsequent to the effective date thereof, the accounts of each of the intervening plaintiffs have been kept and are now kept in full compliance with said order, as required by law.

5. The Interstate Commerce Commission, in response to the request of certain state commissions, entered a further order dated December 27, 1932, for a public hearing with respect to said "First Revised Issue," said case being identified as "Docket No. 25705, Accounting Rules of Telephone Companies." Hearings were thereafter duly held before the Interstate Commerce Commission in April and again in June, 1933, and on July 9, 1934 said Interstate Commerce Commission issued a report setting forth its findings and [fol. 290] conclusions upon the various exceptions and proposed amendments presented at said hearings. A copy of said report is attached to plaintiffs' Bill of Complaint herein, marked Exhibit A, and made a part hereof.

Jurisdiction of said pending proceeding was thereafter and on July 11, 1934, transferred to the defendant, Federal Communications Commission, by virtue of the provisions of Section 604 (b) of the Communications Act. The Commission proceeded therein and on August 16, 1934, issued Telephone Division Order No. 7, a copy of which is hereto attached, marked Exhibit A, and made a part hereof, notifying state commissions and other parties in interest that they might file exceptions or objections to the said report of the Interstate Commerce Commission or suggest amendments to such accounting rules, the case being redocketed and identified as Federal Communications Commission Docket No. 2551. A hearing was thereafter held on November 16, 1934. Thereafter and on May 1, 1935, the Commission issued Telephone Division Order No. 7-B setting forth a proposed Uniform System of Accounts for Telephone Companies entitled "Issue Effective January 1, 1936," and therewith a notice to all parties that they might file exceptions thereto for consideration by the Commission at a conference with the parties, which was held on May 16, 1935.

[fol. 291] Thereafter, on June 19, 1935, the Commission issued the order complained of in this suit, designated Telephone Division Order No. 7-C, prescribing, for the use of telephone companies subject to said Act and having average annual operating revenues exceeding $50,000, a system of accounts entitled "Uniform System of Accounts for Telephone Companies, Issue of June 19, 1935, Effective January 1, 1936," and requiring every such carrier to keep all accounts in conformity therewith on and after January 1, 1936. A copy of said Order No. 7-C, including the text of said "Issue of June 19, 1935" prescribed thereby is attached to plaintiffs' Bill of Complaint herein, marked Exhibit B, and made a part hereof.

6. Intervening plaintiffs are telephone companies having average annual operating revenues exceeding $50,000. Portions of intervening plaintiffs' property have been acquired by them from other public utility companies.

7. For further complaint herein, the intervening plaintiffs adopt as their own, the same as if set forth at length herein, Sections numbered 6, 7 (with the exception of the second paragraph thereof), 8, 9, 10, 11, 12 (with the exception of the second paragraph thereof), 13, 14, 15 and 16

of the Bill of Complaint filed herein by the American Telephone and Telegraph Company, et al., plaintiffs.

[fol. 292] Wherefore, intervening plaintiffs pray:

(1) That a subpœna or subpœnas in chancery issue out of or under the seal of this Honorable Court directed to the defendants as required by law, and that due and proper service of such process and of this Bill of Intervention be forthwith made by filing a copy there in the office of the Secretary of the Commission and another copy in the Department of Justice as in said Urgent Deficiencies Appropriations Act provided, and that thereby the defendants and each of them be required on or before a date to be specified in such subpœena or notice, to appear herein and answer this Bill of Intervention, but not under oath, answer under oath being expressly waived.

(2) That a temporary or interlocutory injunction be entered herein, restraining, enjoining and suspending, until the further order of this court, the operation, execution, effect and enforcement of said order of the Commission.

(3) That pending a hearing upon the aforesaid application for a temporary or interlocutory injunction a preliminary restraining order be issued in terms restraining, enjoining and suspending the operation, execution, effect and enforcement of said order of the Commission until said application for a temporary or interlocutory injunction shall have been heard and determined.

[fol. 293] (4) That after final hearing this court adjudge, order and decree that said order of the Commission is and has at all times been beyond the lawful authority of the Commission, in violation of the legal rights of intervening plaintiffs, and wholly void; and that said order be perpetually vacated, set aside, suspended, and annulled, and the enforcement thereof perpetually restrained and enjoined.

(5) That intervening plaintiffs may have such other and further relief in the premises as to equity and justice may appertain and as may be deemed by this Honorable Court to be adequate and proper under the circumstances.

(Sgd.) C. M. Bracelen, Chas. T. Russell, Alan J. McBean, Solicitors for Intervening Plaintiffs, Address: 195 Broadway, New York, New York.

[fol. 294] *Duly sworn to by Alan J. McBean. Jurat omitted in printing.*

[fol. 295] EXHIBIT "A" TO BILL OF INTERVENTION

Order No. 7

Whereas the Interstate Commerce Commission has heretofore conducted an investigation to determine Accounting Rules for Telephone Companies in that Commission's Docket No. 25705, and

Whereas the Interstate Commerce Commission, on July 9, 1934, decided and rendered its report on Accounting Rules for Telephone Companies, and

Whereas the jurisdiction and authority to fix and promulgate accounting rules for telephone companies was transferred from the Interstate Commerce Commission to the Federal Communications Commission by operation of the Comunications Act of 1934, and

Whereas representatives of certain state commissions or regulatory bodies having jurisdiction over intrastate service rendered by telephone carriers have indicated that they are desirous of being heard on said report of the Interstate Commerce Commission (decided July 9, 1934), and are desirous of filing exceptions and objections and of making suggestions with respect to said report of Interstate Commerce Commission.

It is therefore ordered that representatives of the several states and of the commissions or regulatory bodies thereof having jurisdiction over telephone carriers therein, and all other parties at interest, shall have until October 1, 1934, within which to file exceptions or objections to the report of the Interstate Commerce Commission, rendered in its Docket No. 25705, affecting accounting rules for telephone companies, or to suggest amendments or changes in such accounting rules for telephone companies.

It is further ordered that all such exceptions, objections and suggestions shall be filed in writing and fifteen copies thereof provided within the time herein specified.

Ordered by the Telephone Division of the Federal Communications Commission this the 16th day of August, 1934.

[fol. 296] IN UNITED STATES DISTRICT COURT

[Title omitted]

ANSWER OF THE FEDERAL COMMUNICATIONS COMMISSION—
Filed December 13, 1935

Comes now the defendant, Federal Communications Commission, and answers the bill of complaint herein filed by the American Telephone and Telegraph Company et al., plaintiffs herein.

1. The defendant admits the incorporation of the various plaintiffs as alleged in the bill.

2. The defendant admits that it is an administrative tribunal, created by the Communications Act of 1934, and that it is charged with the administration of said Act.

3. The defendant admits that each of the plaintiffs is, and at all times since the organization of the Federal Communications Commission on July 11, 1934, has been a carrier engaged in communication for hire in interstate or foreign commerce, subject to the provisions of the Communications Act.

4. The defendant admits that prior to the passage of the Communications Act each of the plaintiffs was a common carrier engaged in the transmission of intelligence for hire in interstate commerce, and that each of the plaintiffs was subject to the jurisdiction of the Interstate Commerce Commission under the provisions of the Interstate Commerce Act as amended; that some of the plaintiffs became subject to the jurisdiction of the Interstate Commerce Commission before January 1, 1913, and that some of the plaintiffs became subjject to such jurisdiction on dates as stated in the [fol. 297] petition; that the Interstate Commerce Commission, pursuant to the authority vested in it entered an order dated December 10, 1912, prescribing for certain telephone companies, including plaintiffs, a uniform system of accounts entitled "Uniform System of Accounts for Telephone Companies, First Issue", effective January 1, 1913; that said system was amended in minor respects by subsequent orders of the Interstate Commerce Commission dated December 22, 1914, July 24, 1923, January 8, 1925 and

December 19, 1927; and that by an order dated November 12, 1932, the said Commission prescribed for certain telephone companies, including each of the plaintiffs, a revised system of accounts entitled "Uniform System of Accounts for Telephone Companies, First Revised Issue", effective January 1, 1933.

5. The defendant admits that in response to the request of certain state commissions, the Interstate Commerce Commission entered an order, dated December 27, 1932, for a public hearing with respect to said "First Revised Issue"; that such proceeding was identified as "Docket No. 25705, Accounting Rules of Telephone Companies"; that hearings in said matter were held before the Interstate Commerce Commission in April and June, 1933; that on July 9, 1934, the said Commission issued a report covering various amendments and exceptions presented at said hearings, that a copy of said report is attached as Exhibit A to the bill of complaint, that jurisdiction of said proceeding on Docket No. 25705 of the Interstate Commerce Commission was transferred to the defendant on July 11, 1934, by virtue of provisions of the aforesaid Communications Act; that the defendant, Federal Communications Commission, thereafter exercised jurisdiction in the matter, and on August 16, 1934, issued Telephone Division Order No. 7 notifying the State Commission and other parties in interest that they might file exceptions or objections to the aforesaid report, or suggest amendments to the accounting rules; that the proceeding was identified as Federal Communications Commission Docket No. 2551; that a hearing was held on November 16, 1934, by the Federal Communications Commission; that on May 1, 1935, said Commission, being one of the defendants herein, issued Telephone Division Order No. 7-B setting forth a proposed uniform system of accounts for telephone companies entitled "Issue Effective January 1, 1936"; that therewith a notice to all parties, [fol. 298] including the plaintiffs, was issued, notifying plaintiffs and all other parties that they might file exceptions to said proposed uniform system for consideration of the Commission at a conference which was held on May 16, 1935; that on June 19, 1935, the Federal Communications Commission issued an order designated "Telephone Division Order No. 7-C", prescribing for the use of telephone companies subject to the Communications Act the

uniform system of accounts for telephone companies, issue of June 19, 1935, effective January 1, 1936; and that said system of accounts is embodied in Exhibit B attached to the bill of complaint.

The defendant, further answering paragraph numbered five of the bill of complaint, alleges that while the proceeding on its Docket No. 2551 was pending, and before the uniform system of accounting complained of was prescribed, the plaintiffs submitted, pursuant to Telephone Division Orders No. 7 and No. 7-A, an 83 page statement, dated October 31, 1934, which set forth in detail their position with respect to proposed changes in the uniform system of accounts theretofore applying to the plaintiffs; that there was submitted on the date last named, a statement for and on behalf of various state commissions, prepared by the National Association of Railroad and Utilities Commissions, which set forth in detail the views of said commissions respecting amendments to the uniform system of accounts; that on the same date there was submitted to the defendant commission a twelve page memorandum, with letter of transmittal, on behalf of thirteen state commissions, said letter being dated October 31, 1934; that the Railroad Commission of the State of California submitted a thirteen page memorandum dated September 23, 1934, stating its views respecting proposed changes in the uniform system of accounts; that on September 26, 1934, the Michigan Public Utilities Commission submitted its views with respect to the same subject in an eleven page memorandum, that on July 21, 1934, the Peoples Counsel of the District of Columbia, Public Utilities Commission, submitted his view on the same subject matter in a 31 page paper; that on October 29, 1934, the United States Independent Telephone Association submitted a ten page memorandum, dated October 29, 1934, setting forth its views with respect to the things under consideration on the docket mentioned; that each and every one of the papers and statements [fol. 299] submitted, as aforesaid, was carefully considered by the Commission, and by its proper department, at a series of conferences held subsequent to November 16, 1934; that on February 18, 19 and 20, and on April 24 and on May 1, all in the year 1935, conferences were held with

representatives of the state commissions pursuant to the provisions of Section 220 (i) of the Communications Act of 1934, at which the subject under consideration on Docket No. 2551 was thoroughly examined and considered; that on May 1, 1935, the defendant issued Telephone Division Order No. 7-B, setting forth a proposed uniform system of accounts for telephone companies entitled "Issue Effective January 1, 1936"; that thereupon the Commission issued a notice to all parties, including plaintiffs, inviting them to file exceptions, if they cared to do so, for consideration of the Commission at a conference with the plaintiffs and other parties, which was held on May 16, 1935, that at said conference the plaintiffs submitted a 22 page statement of exceptions to the proposed system, dated May 15, 1935; that other parties submitted memoranda; that such exceptions and memoranda were considered by the two-day conference held by the Federal Communications Commission on May 16 and 17, 1935; that at such conference the American Telephone and Telegraph Company, and other plaintiffs, were represented by their attorneys and their accountants; that thereafter, and on May 24, 1935, the plaintiffs filed with the Commission, pursuant to understanding had at the May 16 conference, a 78 page statement of exceptions to the proposed system of accounts; that others filed exceptions; that these exceptions were given careful consideration by the Telephone Division of the Federal Communications Commission before the entry of Order No. 7-C, which the plaintiffs propose to vacate, set aside, suspend, and annul.

6. The defendant denies that Order No. 7-C is unlawful and void; that it is contrary to Section 404 of the Communications Act; that it is in violation of the rights of plaintiffs under the due process provisions of the Constitution; and the defendant denies that said Order No. 7-C is unlawful for the failure of the defendant to make a report in writing, and to make findings and conclusions, or for any other reason whatsoever.

[fol. 300] 7. The defendant admits that the system of accounts prescribed by Order No. 7-C requires plaintiffs to record their properties upon their books of account and records at their "original cost" which is defined in said system as "the actual money cost of (or the current money value of any consideration other than money exchanged

for) property at the time when it was first dedicated to the public use, whether by the accounting company or by a predecessor public utility"; but defendant states that the Uniform System of Accounts contains other provisions as follows:

100.4. Telephone plant acquisition adjustment.—(A) This account shall include the difference between (a) the amount of money actually paid (or the current money value of any consideration other than money exchanged) for telephone plant acquired, plus preliminary expenses incurred in connection with the acquisition; and (b) the original cost (note instruction 3-S.1) of such plant, governmental franchises and similar rights acquired, less the amounts of reserve requirements for depreciation and amortization of the property acquired, and amounts of contributions to the predecessor company or companies for construction and acquisition of such property. If the actual original cost is not known, the entries in this account shall be based upon an estimate of such cost. (Note also instruction 21.)

(B) This account shall be subdivided according to the character of the amounts contained therein. In addition to a copy of the journal entry recorded to open the account, the company shall file with this Commission statements showing the basis of the computation of amounts included therein. The detailed records supporting these statements shall be retained permanently by the company.

(C) The amounts recorded in this account with respect to each property acquisition shall be disposed of, written off, or provision shall be made for the amortization thereof in such manner as this Commission may direct. (Note also instruction 21.)

276. Telephone plant acquired.—This account shall be charged temporarily with the cost of acquisition (i. e., amount of money actually paid or the current money value of any consideration other than money exchanged for telephone plant, together with the preliminary expenses incurred in connection with the acquisition) of telephone plant pending distribution to the primary telephone plant accounts and to other accounts. (Note also instruction 21 and 82.)

The defendant states that among the rules prescribed by Order No. 7-C as a part of the Uniform System of Accounts, the following appears:

2. Records.—(A) The company's records shall be kept with sufficient particularity to show fully the facts pertaining to all entries in these accounts. Where the full information is not recorded in the general books the entries therein shall be supported by other records in which the full details shall be shown and the general book entries shall contain sufficient reference to the detail records to permit ready identification. The detail records shall be filed in such manner as to be readily accessible for examination by representatives of this Commission.

• • • • • • •

[fol. 301] (D) As of the effective date of this system of accounts, the several accounts prescribed herein shall be opened by transferring thereto the balances carried in the accounts previously maintained by the company. Copies of the journal entries recorded to effect these transfers shall be filed with this Commission. The company is authorized to make such subdivisions, reclassifications, or consolidations of such balances as are necessary to meet the requirements of this system of accounts.

21. Telephone plant acquired.—(A) When property in use in telephone service (note instruction 3-AA) is acquired, the amount of money actually paid (or the current money value of any consideration other than money exchanged) for the property (together with preliminary expenses incurred in connection with the acquisition) shall be charged to account 276, "Telephone plant acquired." (Note also account 139.)

(B) The accounting for the acquisition of the plant shall then be completed as follows:

(1) The original cost, estimated if not known, (note instruction 3-S.1) of telephone plant, governmental franchises and other similar rights acquired shall be charged to the telephone plant accounts, account 100.2, "Telephone plant under construction", and account 100.3, "Property held for future telephone use", as appropriate, and credited to account 276. When the actual original cost cannot

be determined and estimates are used, the company shall be prepared to furnish this Commission with the particulars of such estimates.

(2) The amounts of the reserve requirements for depreciation and amortization of the plant acquired shall be credited to account 171, "Depreciation reserve", and account 172, "Amortization reserve", and debited to account 276.

(3) The amount of contributions to the predecessor company or companies for construction and acquisition of the telephone plant acquired shall be credited to account 175, "Contributions of telephone plant", and debited to account 276 on the books of the accounting company.

(4) The amount remaining in account 276, "Telephone plant acquired", applicable to the plant acquired, shall upon completion of the entries provided in the foregoing paragraphs (1), (2), and (3), be debited or credited, as appropriate, to account 100.4, "Telephone plant acquisition adjustment", except that when any amount thus chargeable to account 100.4 applies to duplicate or other telephone plant which will be retired by the vendee in the reconstruction of the acquired property and its consolidation with previously owned property, the accounting for the amount applicable to such plant shall be submitted to this Commission for consideration and approval.

(C) Journal entries recording the acquisition of a complete telephone system, a complete exchange, a complete toll system, or other telephone plant where the consideration paid is $25,000 or more, shall be submitted to this Commission for consideration and approval. The text of such entries shall give a complete description of the property acquired and the bases upon which the amounts of the entries have been determined.

The defendant states that the foregoing parts of the Uniform System of Accounts and all the matters and things covered by the references therein are found in Exhibit B attached to the Bill of Complaint.

[fol. 302] The defendant states that it has no knowledge respecting the amount of property acquired by the plaintiffs before or after January 1, 1913, and that it has no

knowledge respecting the form and manner in which the plaintiffs have recorded their property investments covering property acquired either before or since January 1, 1913; but the defendant denies that the definition of original cost taken in connection with other provisions of the Uniform System of Accounts will require the plaintiffs so to restate, as of January 1, 1936, their property investment accounts by eliminating therefrom the recorded cost or investment of the plaintiffs in property theretofore acquired by them from another public utility; and the defendant denies that any property acquired by the plaintiffs after July 1, 1936, shall be carried in the property investment accounts of the plaintiffs at an amount different from that which the plaintiffs may actually pay for the property acquired; and the defendant alleges the fact to be that when the entire Uniform System of Accounts as exemplified by Exhibit B of the plaintiffs is applied, the plaintiffs will be able to keep a legitimate record of all of their transactions.

The defendant further answering paragraph 7 of the Bill of Complaint states that the account numbered 100.4 mentioned by the plaintiffs is above quoted herein, including sub-divisions (A), (B) and (C) and that as aforesaid the account 100.4 and all of its parts are found in Exhibit B attached to the Bill of Complaint; and the defendant states that the matter of construing and interpreting the provisions of said account No. 100.4 (A), (B) and (C) is for the court and not for the plaintiffs; but the defendant denies that the requirements of said account are so entirely contrary to fundamental principles of correct accounting and so arbitrary and unreasonable as to amount to an abuse of the Commission's power; and the defendant denies that the requirements made in said account are beyond the statutory power and authority of the Commission; and the defendant denies that the requirements mentioned are illegal and void for reasons alleged by the plaintiffs or for any other good and sufficient reasons.

The defendant yet pleading to paragraph 7 of the Bill of Complaint states that the construction and interpretation of the provisions in the Uniform System of Accounts covered by the aforesaid Order No. 7-C, respecting the expense of depreciation and concerning the portion of property [fol. 303] invested to be recorded in account No. 100.4 are for the court and not for the plaintiffs; but nevertheless, the

defendant denies that the Uniform System of Accounts operates to prevent the plaintiffs from charging of proper expenses of depreciation whether with respect to that portion of their property investment included in account No. 100.4 or in any other account.

The defendant answering sub-paragraph (a), (b) and (c) of paragraph 7 of the Bill of Complaint denies that the requirements of the Uniform System of Accounts will necessitate the keeping of the plaintiffs' property investment accounts on a basis which will reflect neither the fact of their actual investment nor the value thereof; and the defendant denies that the Uniform System of Accounts would require plaintiffs to conceal the amount of actual investment made by them.

The defendant denies that the Uniform System of Accounts would operate to require the plaintiffs to write off any portion of their actual investment; that it would prevent plaintiffs from recording in their expense accounts any legitimate expense of depreciation.

The defendant answering sub-paragraph (d) of paragraph 7 of the Bill of Complaint states that said sub-paragraph states no cause of action nor any part of a cause of action; but the defendant denies that the requirements of the Uniform System of Accounts are impracticable of application to the accounting of the plaintiffs; and the defendant states that difficulty and expense in applying the Uniform System supply no reason for nullifying the system.

The defendant pleading to sub-paragraph (e) of paragraph 7 of the Bill of Complaint alleges that the same states no cause of action or any part of a cause of action and alleges that the Communications Act of 1934 authorizes the defendant to prescribe and to put into force and effect the Uniform System of Accounts as set out in Exhibit B attached to the Bill of Complaint.

The defendant answering sub-paragraph (f) of paragraph 7 of the Bill of Complaint states that the construction and interpretation of Account No. 100.4 is for the court and not for the plaintiffs; and the defendant also states that the authority of the Federal Communications Commission is established by law and that the determination of the authority of said Commission is for the court and not for the plaintiffs; and the defendants state that said sub-paragraph (f) of said paragraph 7 states no cause of action or any

[fol. 304] part of cause of action and should be eliminated from the Bill of Complaint.

The defendant answering sub-paragraph (g) of paragraph 7 of the Bill of Complaint denies that the requirements of the Uniform System of Accounts is inconsistent with or contrary to Sections 213 (c) and 219(a) of the Communications Act of 1934; and the defendant denies that the said requirements are in violation of Section 4 (i) of said Act; and on the other hand the defendant alleges that the sections mentioned confer jurisdiction on the Federal Communications Commission which may be exercised in connection with the authority of said Commission under Section 220 of said Act.

8. The defendant answering paragraph 8 of the Bill of Complaint states that the account entitled "Contributions of Telephone Plant" is a part of the Uniform System of Accounts appearing in writing in Exhibit B, attached to the plaintiffs' Bill of Complaint, and that the construction and interpretation of said account as so appearing in writing is for the court and not for the plaintiffs; however, the defendant denies that the system of accounts mentioned in said paragraph requires the plaintiffs' accounts to show any liability for any contribution not received by the plaintiffs, and the defendant denies that the requirements mentioned in said paragraph 8 are arbitrary and unreasonable and denies that they are illegal and void because of the lack of statutory power and authority in the Commission, or for any other reason whatsoever.

9. The defendant answering paragraph numbered 9 of the Bill of Complaint alleges that said paragraph does not state any cause of action, nor any part of a cause of action; but the defendant denies that the dividing line between the classifications mentioned in said paragraph 9 are so indefinite and ambiguous as to be impossible for plaintiffs' understanding; and the defendant denies that it is without authority to prescribe such classification and to exact obedience thereto; and, furthermore, the defendant states that Rule No. 9 in the Uniform System of Accounts provides as follows, to wit:

"To the end that uniformity of accounting may be maintained, the company shall submit all questions of doubtful interpretation of the prescribed accounting to this Commission for consideration and decision."

The defendant further answering said paragraph 9 denies that the system of accounts prescribed by the Commission would require the plaintiffs to make entries in their accounts at their peril, or at the risk of penalties prescribed [fol. 305] by the Communications Act of 1934, or any other law in force and effect; and furthermore the defendant states that where entries in the prescribed accounts are erroneously made in good faith, the penalty provisions of the aforesaid Act do not apply.

10. The defendant answering paragraph 10 of the Bill of Complaint states that Account No. 100.3 therein mentioned exists in writing and is set out in plaintiffs' Exhibit B, attached to the Bill of Complaint; that the construction and interpretation thereof are for the court, and not for the plaintiffs; but the defendant denies that the account mentioned prevents the recording of depreciation expense with respect to property under Account 100.3 for the time such property is included in said account or for any other time or under any other circumstance where the plaintiffs would be lawfully entitled to record the expense of depreciation; and the defendant denies that the requirements mentioned in paragraph 10 of the Bill of Complaint are contrary to fundamental principles of correct accounting or are arbitrary or unreasonable, or are illegal and void for the reasons mentioned in said paragraph, or for any other reasons.

11. The defendant, answering paragraph 11 of the Bill of Complaint, admits that the Uniform System of Accounts requires that all charges to plant investment, income, operating revenue, and operating expense accounts, shall be just and reasonable, and that any payments by plaintiffs in excess of just and reasonable charges respecting the matters mentioned, shall be charged against income; but the defendant denies that such requirement is contrary to the fundamental principles of correct accounting, and denies that it is arbitrary and unreasonable; and the defendant denies that the plaintiffs would of necessity be required to make any charges, under the circumstances stated, at their peril or at the risk of penalties prescribed by the Communications Act; and the defendant denies that it is without authority to prescribe the requirement mentioned, but on the other hand the defendant states that the requirement in

the Uniform System of Accounts, whereby charges to investment and other accounts mentioned in paragraph 11 of the Bill of Complaint shall be just and reasonable, is valid; and, furthermore, the defendant alleges that all any carrier would of necessity be required to do in the premises to escape penalties under the Communications Act of 1934, would be to make a proper effort to comply with the Act and the Accounting requirements; that under Section 220 (g) of [fol. 306] the Act the Commission may approve, as well as prescribe, accounts, or the form of accounts; that practice before the Interstate Commerce Commission respecting such matters became settled prior to the passage of the Communications Act; that accounting reports filed by carriers before the Interstate Commerce Commission have been, and are, there subjected to consideration, and then to proper order, in all such matters, whether favorable or unfavorable to the carrier; that the said practice would prevail before the Federal Communications Commission; that no carrier attempting to comply with the accounting requirements prescribed by Order No. 7-C, mentioned in the Bill of Complaint and in this answer, could or would come under and be subjected to the penal provisions of the Communications Act until the rejection of its accounting report, when offered by a carrier, and then not until the Commission, in due course of business, might make and enter an order against the carrier specifying with respect to requirements in the particular instance and matter necessary to make the accounting report under consideration at the time conform with prescribed or approved accounting; and the defendant further states that under Instruction No. 9 in the accounting system, being the rule mentioned and stated in paragraph number 9 of this answer, no carrier could be subjected to the penal provisions of the Act unless such carrier, of its own volition, should refuse to take advantage of the provisions of said rule number 9.

12. The defendant answering paragraph 12 of the Bill of Complaint states that it is without knowledge of any instance, circumstance or occasion upon or under which the plaintiffs might use any accounting statements made to any administrative or regulatory body in complying with the demand of tax authorities and other governmental agencies; and the defendant denies that the order complained of in paragraph 12 of the Bill of Complaint makes it impossible

for plaintiffs to keep accounts adequate for the purpose of making reports to tax authorities and other governmental agencies and for making true representations to stockholders, officers and directors, or to anyone else whomsoever.

The defendant further answering paragraph 12 of the Bill of Complaint denies that the order complained of therein would result in the publication of financial statements radically different from what they have been or should be; that such statements would be contradictory of plaintiffs' [fol. 307] respective financial structures or status; that such statements would seriously impair plaintiffs' credit; or that such statements would take the property of the plaintiffs without due process of law.

13. The defendant answering paragraph 13 of the Bill of Complaint denies that the provisions of the "Issue of June 19, 1935" therein mentioned are so constituted that such provisions are interdependent and non-severable; and it denies that said "Issue of June 19, 1935" and Order No. 7-C prescribing the same are illegal and void in their entirety upon the grounds alleged in the Bill of Complaint or upon any other grounds.

14. The defendant answering paragraph 14 of the Bill of Complaint alleges that the same states no cause of action nor any part of a cause of action; that Order No. 7-C mentioned in said paragraph of the said Bill of Complaint is in writing and appears in the Exhibit B attached to the Bill of Complaint, and that the ascertainment of the requirements thereunder is for the court by construction and interpretation, and not for the plaintiffs; and further the defendant states that expense attributable to the preparation of accounts in compliance with the order is no defense against the requirements thereof; and defendant denies that the requirement mentioned in said paragraph numbered 14 is arbitrary or unreasonable or beyond the statutory power and authority of the Commission.

15. The defendant, answering paragraph 15 of the Bill of Complaint, denies that in the premises thereby covered the plaintiffs have no adequate remedy at law, and denies that they will suffer irreparable injury and damage in the absence of the relief for which they pray; and in this connection the defendant alleges that the plaintiffs have failed

to notice that they might seek the remedy allowed them under Section 220 (g) of the Communications Act of 1934, under which the Federal Communications Commission may approve accounts reported as well as prescribe accounts in advance; that the plaintiffs have failed to notice that they might petition the Commission respecting the manner and form of reporting accounts under the general accounting order and requesting such order as might be desired in the premises; and that the plaintiffs have failed to take notice of Instruction No. 9 among the rules in the Uniform System of Accounts, under which they might submit doubtful questions respecting prescribed accounting to the Commission for further consideration and decision.

[fol. 308] The defendant further answering paragraph 15 of the Bill of Complaint states that the plaintiffs have failed to notice that under Section 5 (e) of the Communications Act of 1934 they might have demanded a rehearing and that they might have done so under Section 405(c) of said Act; and the defendant states that by failing to request a rehearing the plaintiffs have not pursued and exhausted their remedies under the law for correcting the matters and things of which they now complain.

The defendant further answering states that the plaintiffs have failed to notice that they might, when having reason to believe that an item should be carried in a different account from that by which it is required to be carried under the Uniform System of Accounts, petition the Commission for relief respecting the manner and form of reporting such item.

16. The defendant answering paragraph numbered 16 of the Bill of Complaint states that the essentials of said paragraph have been heretofore fully covered by the foregoing parts of this answer; however, the defendant denies that when the Uniform System of Accounts becomes effective the plaintiffs would be subjected to a multiplicity of suits and to criminal prosecutions for the recovery and assessment of fines and penalties under Sections 220, 501, and 502 of the Communications Act of 1934, unless the plaintiffs themselves should arbitrarily choose to be sued and to be prosecuted.

17. The defendant, further answering the Bill of Complaint, and particularly that part of it contained in para-

graph 7, subparagraph "e", denies that the requirements referred to in said paragraph "e", compel the plaintiffs, or will, on and after January 1, 1936, compel the plaintiffs to make radical changes in their completed accounts; and the defendant denies that the Uniform System of Accounts prescribes any retroactive changes in accounts which have been lawfully kept, although said system may, and to an extent does, require a reclassification of items of account.

18. The defendant, further answering the Bill of Complaint, alleges that the order of which the plaintiffs complain, was entered, as the date thereof indicates, on June 19, 1935, that the Uniform System of Accounts prescribed by the Federal Communications Commission, being authorized and approved by said order on the date thereof, was forthwith, and along with said order, served on the plain-
[fol. 309] tiffs, that thereafter the plaintiffs took none of the steps, and availed themselves of none of the procedure, hereinabove mentioned, to bring any matter or thing of inaccuracy, inequity, or invalidity, to the attention of the Federal Communications Commission, to the end and for the purpose that any matter of inaccuracy, inequity, or invalidity, might be amended, corrected, or otherwise modified, or even annulled, rejected, suspended, and set aside; and, furthermore, without in the interim giving the Federal Communications Commission any opportunity to consider the things of which the plaintiffs complain in the Bill of Complaint, they waited to bring this suit for a period of 156 days; and until after a time when the Uniform System of Accounts attacked could be modified so as to become effective on January 1, 1936, whereas if the system does not become effective on that date, the operation of it, or any part of it which may not be enjoyed in these proceedings, will be postponed for another additional calendar year; and upon the facts stated in this paragraph, and to some extent elsewhere in the answer, the defendant pleads that the plaintiffs have been guilty of laches, which ought to defeat their right to the relief and remedy for which they pray.

19. The defendant states that there is no equity in the Bill of Complaint.

20. The defendant, further answering the Bill of Complaint, denies each and every allegation therein contained,

excepting the matters and things heretofore specifically admitted, qualified, or otherwise answered.

Wherefore, the defendant prays that the Bill of Complaint be dismissed, and that the defendant be discharged.

Federal Communications Commission, by Albert E. Stephan, W. D. Humphrey. Hampson Gary, General Counsel; Frank Roberson, Assistant General Counsel, of Counsel.

[fol. 310] *Duly sworn to by Paul A. Walker. Jurat omitted in printing.*

[fol. 311] IN UNITED STATES DISTRICT COURT

[Title omitted]

PETITION OF THE NATIONAL ASSOCIATION OF RAILROAD AND UTILITIES COMMISSIONERS FOR LEAVE TO INTERVENE—Filed December 16, 1935

To the Honorable Judges of the District Court of the United States for the Southern District of New York:

Respectfully represents the National Association of Railroad and Utilities Commissioners as follows:

I

Said National Association of Railroad and Utilities Commissioners is a voluntary Association including in its membership the members of the railroad commissions, public service commissions, and other regulatory commissions and boards of the several States of the United States, except the States of Delaware and New York.

II

That most of said State regulatory commissions and boards exercise regulatory jurisdiction over telephone companies in their respective States, including jurisdiction over the accounts of such companies.

[fol. 312] III

That Section 220 (i) of the Communications Act of 1934 provides as follows:

"(i) The Commission, before prescribing any requirements as to accounts, records, or memoranda, shall notify each State commission having jurisdiction with respect to any carrier involved, and shall give reasonable opportunity to each such commission to present its views, and shall receive and consider such views and recommendations."

IV

That Section 410 (b) of said Communications Act provides in part as follows:

"(b) The Commission may confer with any State commission having regulatory jurisdiction with respect to carriers, regarding the relationship between rate structures, accounts, charges, practices, classifications, and regulations of carriers subject to the jurisdiction of such State commission and of the Commission * * *."

V

That on August 16, 1934 the Federal Communications Commission had under consideration the then existing Uniform System of Accounts for Telephone Companies, which had been prescribed by the Interstate Commerce Commission when that Commission exercised jurisdiction over such companies, by its order dated November 12, 1932, and objections thereto and recommendations for changes therein, which had been filed by various State commissions with said Interstate Commerce Commission, together with a report of said Interstate Commerce Commission, upon such objections and recommendations, which had been made in a proceeding known as I. C. C. Docket 25705, which said proceeding had been transferred to said Federal Communications Commission under the provisions of Section 604(b) of said Communications Act, and was then pending before said last named Commission; and that said Federal Communications Commission thereupon issued Telephone Division Order No. 7, giving notice to State commissions and others that they might file exceptions or objections to said report, or suggest amendments to the accounting rules con-

tained in said Uniform System of Accounts, and under consideration in said before mentioned proceeding.

[fol. 313] VI

That thereafter on October 31, 1934 said National Association of Railroad and Utilities Commissioners, acting on behalf of 42 State commissions represented in its membership, became a party to said proceeding, and filed suggested amendments to the accounting rules contained in said Uniform System of Accounts, and thereafter, in a hearing held before said Commission on November 16, 1934, was heard in oral argument in support of said recommendations; and that thereafter said State commissions further presented their views respecting said recommendations at an informal conference.

VII

That thereafter on June 19, 1935 said Federal Communications Commission issued Telephone Division Order No. 7 (c) prescribing the Uniform System of Accounts for Telephone Companies, effective January 1, 1936, which said order is sought to be enjoined and set aside in this proceeding.

VIII

That said Uniform System of Accounts contains many provisions which had been recommended by said National Association of Railroad and Utilities Commissioners on behalf of said 42 State commissions.

IX

The said National Association of Railroad and Utilities Commissioners at its last annual convention, on October 18, 1935, adopted a resolution as follows:

"Whereas, the Interstate Commerce Commission, while vested with jurisdiction over the accounts of telephone companies engaged in interstate Commerce, prescribed a system of accounts for telephone companies, which system was also prescribed or approved for use in various States as the basis for reports to the respective State regulatory commissions; and

[fol. 314] Whereas, Said Interstate Commerce Commission thereafter prescribed a revised system of accounts

for telephone companies, based upon the aforesaid system, to be known as "Uniform System of Accounts for Telephone Companies," which system became effective January 1, 1933; and

Whereas, Various State regulatory commissions prior to the taking effect of the said uniform system of accounts protested against various provisions contained therein and requested amendment of the same; and

Whereas, After a hearing upon said protests following the enactment of the Communications Commission Act of 1934 but before the same took effect, the Interstate Commerce Commission in its docket No. 25705 filed a report dealing with said protests; and

Whereas, Following the organization of the Federal Communications Commission, said Commission, by order No. 7 of its Telephone Division, provided that the State regulatory commissions and other interested parties should have until October 1, 1934 to file exceptions and objections to said report of the Interstate Commerce Commission, which time upon request of representatives of this Association was later extended until November 1, 1934; and

Whereas, Exceptions and objections were prepared by the accounting representatives of various State regulatory commissions, working together, which were distributed to all the commissions of the States represented in this Association, and were generally approved and filed on behalf of State regulatory commissions represented in this Association; and

Whereas, Said exceptions and objections were also considered by a conference of representatives of the various State commissions held at Washington, D. C., on the day preceding the 1934 convention of this Association and were approved by said conference; and

Whereas, At a hearing thereafter held before the Telephone Division of said Federal Communications Commission, said exceptions and objections were supported by the General Solicitor of this Association under instructions from the commissions of forty-two States; and

Whereas, Following said hearing the Federal Communications Commission, through its Telephone Division, called a conference of representatives of State commissions and of telephone utilities for discussion and consideration of

the provisions to be contained in said proposed Uniform System of Accounts, at which conference the State commissions were represented by officers of this Association and by the accountants who had prepared said exceptions and objections; and

Whereas, Said exceptions and objections were thereupon fully considered and the Uniform System of Accounts for Telephone Companies theretofore promulgated by the Interstate Commerce Commission was thereupon amended and revised; and

Whereas, The accounting representatives of the State commissions represented in this Association participating in said conference concurred in such amendments and revision; and

[fol. 315] Whereas, Said revised Uniform System of Accounts has since been promulgated by the Federal Communications Commission through its Telephone Division by its order dated June 19, 1935, to be known and designated as 'Uniform System of Accounts for Telephone Companies, issue of June 19, 1935, effective January 1, 1936'; and

Whereas, It is highly desirable that accounting regulations prescribed for the use of companies subject to the jurisdiction of both Federal and State authorities shall be prepared in cooperative conferences and shall be prescribed by both Federal and State authorities whenever that shall be possible, so that conflicting and diverse requirements may be avoided; Therefore be it

Resolved, That this Association recommends to the several State commissions represented in this Association, which exercise jurisdiction over the accounts of telephone companies that they respectively adopt and prescribe for State application the aforesaid Uniform System of Accounts for Telephone Companies, prescribed as aforesaid by Federal Communications Commission.

Resolved Further, That this Association, on behalf of the State commissions represented in its membership, hereby expresses the appreciation of said State commissions of the fine cooperative spirit displayed by the Federal Communications Commission in its proceedings with respect to said Uniform System of Accounts."

X

That since the adoption of said resolution some of said State commissions have adopted said uniform system of

accounts for application within their respective States, and the same is in process of consideration and adoption in other States by the commissions thereof.

XI

That said National Association of Railroad and Utilities Commissioners is interested in said Telephone Division Order No. 7 (c) of said Federal Communications Commission and in this proceeding, which has been brought to enjoin, annul and set aside the same, and desires to be admitted as an intervening party defendant, so that it may be heard by this court in defense of said order; and that, as a party to the aforesaid proceeding before said Federal Communications Commission, under Section 212 of the Judicial Code it has a right to intervene herein.

[fol. 316] Wherefore said National Association of Railroad and Utilities Commissioners prays that it may be permitted to intervene in this proceeding, with the right to file its answer herein, and to be heard as a party upon all issues presented for decision herein.

John E. Benton, General Solicitor, National Association of Railroad and Utilities Commissioners, Clyde S. Bailey, Assistant General Solicitor, National Association of Railroad and Utilities Commissioners, 806-808 Earle Building, Washington, D. C.

Duly sworn to by John E. Benton. Jurat omitted in printing.

[fol. 317] In United States District Court

[Title omitted]

Order Granting the Petition of the National Association of Railroad and Utilities Commissioners for Leave to Intervene—Filed December 16, 1935

In the above entitled proceeding the National Association of Railroad and Utilities Commissioners having this day presented its petition for leave to intervene herein as a party defendant, with the right to file its answer herein,

and to be heard as a party upon all issues presented for decision herein, and it appearing that said National Association of Railroad and Utilities Commissioners was a part to the proceeding before the Federal Communications Commission in which the Order was made which is involved in this proceeding, it is

Ordered that said petition of said National Association of Railroad and Utilities Commissioners be granted, and that it have leave to appear herein as a party defendant, and to file its answer and to be heard as a party herein.

Jno. C. Knox, United States District Judge.

[fol. 318] In United States District Court

[Title omitted]

Answer of the National Association of Railroad and Utilities Commissioners—Filed December 16, 1935

Comes now the National Association of Railroad and Utilities Commissioners, appearing as an intervening party defendant by leave of Court, and makes answer to the plaintiff's bill of complaint, as follows:

Said National Association of Railroad and Utilities Commissioners makes reference to the answer of the Federal Communications Commission this day filed herein, and adopts said answer as its own, admitting the allegations of fact contained in the plaintiff's bill which are admitted in said answer, and denying each such allegation which is in said answer denied.

Wherefore said intervening defendant prays that said bill of complaint may be dismissed.

John E. Benton, Clyde S. Bailey, Attorneys for National Association of Railroad and Utilities Commissioners.

Duly sworn to by John E. Benton. Jurat omitted in printing.

[fol. 319] IN UNITED STATES DISTRICT COURT

[Title omitted]

ANSWER OF THE FEDERAL COMMUNICATIONS COMMISSION TO THE BILL OF COMPLAINT OF OHIO ASSOCIATED TELEPHONE COMPANY ET AL, ADDITIONAL PLAINTIFFS—Filed December 23, 1935

Comes now the defendant, Federal Communications Commission, and answers the Bill of Complaint herein filed by the additional plaintiffs, Ohio Associated Telephone Company and others.

1. The defendant admits the incorporation of the plaintiffs named in paragraph 1 of the Bill of Complaint as stated therein.

2. The defendant, Federal Communications Commission, admits that it is an administrative tribunal created by the Communications Act of 1934; that it is charged with the administration of said Act; and that it was organized on July 11, 1934, as alleged in pragraph 2 of the Bill of Complaint.

3. The defendant admits that each of the additional plaintiffs is, and at all times since the effective date of the said Communications Act has been, a carrier engaged in communication for hire in interstate and foreign commerce, and that each of said plaintiffs is subject to the provisions of said Act as alleged in paragraph 3 of the Bill of Complaint.

[fol. 320] 4. The defendant admits the commencement of this suit by the original plaintiffs as alleged in paragraph 4 of the Bill of Complaint.

5. The defendant, answering paragraph 5 of the Bill of Complaint, states that the allegations contained therein are matters which the court will determine for itself without the aid of pleadings.

6. The defendant admits that on August 16, 1934, the Communications Commission issued Telephone Division Order No. 7 notifying state commissions and other parties in interest, including the additional plaintiffs, that they

might file exceptions and objections to the report of the Interstate Commerce Commission dated July 9, 1934, in a proceeding identified as Docket No. 25,705, Accounting Rules of Telephone Companies and also notifying additional plaintiffs and others that they might suggest amendments to such accounting rules; that the case was redocketed and identified as Federal Communications Commission Docket No. 2551; that a hearing was thereafter held on November 16, 1934; that on May 1, 1935, the Commission issued Telephone Division Order No. 7-B setting forth a proposed uniform system of accounts for telephone companies entitled Issue Effective January 1, 1936; that therewith the Commission issued a notice to all parties, including the additional plaintiffs, that they might file exceptions thereto for consideration by the Commission at a conference with the parties which was held on May 16, 1935; and that said plaintiffs appeared at said conference and filed exceptions to the proposed uniform system of accounts for telephone companies.

The defendant admits that on June 19, 1935, the Communications Commission issued the Order complained of in this suit designated Telephone Division Order No. 7-C prescribing for the use of telephone companies subject to the aforesaid Communications Act and having average annual operating revenues exceeding $50,000, a system of accounts [fol. 321] entitled "Uniform System of Accounts for Telephone Companies, Issue of June 19, 1935, Effective January 1, 1936," and requiring every such carrier to keep accounts in conformity therewith on and after January 1, 1936; that a copy of said Order No. 7-C, including the text of said issue of June 19, 1935, prescribed thereby, is filed with the original Bill of Complaint of the American Telephone and Telegraph Company et al in this cause; and that each of the additional plaintiffs is a telephone company having average annual operating revenues exceeding $50,000, and is subject to the provisions of said Order No. 7-C.

7. The defendant admits that the additional plaintiffs are parties in interest, or were parties in interest, in the proceeding before the Communications Commission, docketed and identified as Federal Communications Commission Docket No. 2551.

8. The defendant denies that its Order No. 7-C is unlawful and void; that it is contrary to Section 404 of the Com-

munications Act of 1934; and that it is in violation of the rights of the additional plaintiffs under constitutional provisions for the reason that with respect to said Order No. 7-C the Commission made no report in writing, no findings and no statement of its conclusions, or for any other reason whatsoever; and on the other hand, the defendant alleges that the Uniform System of Accounts followed by said Order No. 7-C constitutes sufficient findings and conclusions in the matter under consideration in Federal Communications Commission Docket No. 2551; furthermore, the defendant states that no findings and no conclusions other than those appearing in said Order No. 7-C and in the Uniform System of Accounts authenticated thereby, were necessary in the premises.

9. The defendant, answering paragraph 9 of the Bill of Complaint of the additional plaintiffs, admits that the System of Accounts prescribed by Order No. 7-C requires the [fol. 322] additional plaintiffs to record their properties upon their books of account and records at their original cost which is defined in said System as the actual money cost of (or current money value of any consideration other than money exchanged for) property at the time when it was first dedicated to the public use, whether by the accounting company or by a predecessor public utility; but the defendant states that the Uniform System of Accounts contains other provisions as follows:

100.4. Tlephone plant acquisition adjustment.—(A) This account shall include the difference between (a) the amount of money actually paid (or the current money value of any consideration other than money exchanged) for telephone plant acquired, plus preliminary expenses incurred in connection with the acquisition; and (b) the original cost (note instruction 3-S. 1) of such plant, governmental franchises and similar rights acquired, less the amounts of reserve requirements for depreciation and amortization of the property acquired, and amounts of contributions to the predecessor company or companies for construction and acquisition of such property. If the actual original cost is not known, the entries in this account shall be based upon an estimate of such cost. (Note also instruction 21.)

(B) This account shall be subdivided according to the character of the amounts contained therein. In addition to

a copy of the journal entry recorded to open the account, the company shall file with this Commission statements showing the basis of the computation of amounts included therein. The detailed records supporting these statements shall be retained permanently by the company.

(C) The amounts recorded in this account with respect to each property acquisition shall be disposed of, written off, or provision shall be made for the amortization thereof in such manner as this Commission may direct. (Note also instruction 21.)

276. Telephone plant acquired.—This account shall be charged temporarily with the cost of acquisition (i.e., amount of money actually paid or the current money value of any consideration other than money exchanged for telephone plant, together with the preliminary expenses incurred in connection with the acquisition) of telephone plant pending distribution to the primary telephone plant accounts and to other accounts. (Note also instructions 21 and 82.)

The defendant states that among the rules prescribed by Order No. 7-C as a part of the Uniform System of Accounts, the following appears:

2. Records.—(A) The company's records shall be kept with sufficient particularity to show fully the facts pertaining to all entries in these accounts. Where the full infor- [fol. 323] mation is not recorded in the general books the entries therein shall be supported by other records in which the full details shall be shown and the general book entries shall contain sufficient reference to the detail records to permit ready identification. The detail records shall be filed in such manner as to be readily accessible for examination by representatives of this Commission.

* * * * * * *

(D) As of the effective date of this system of accounts, the several accounts prescribed herein shall be opened by transferring thereto the balances carried in the accounts previously maintained by the company. Copies of the journal entries recorded to effect these transfers shall be filed with this Commission. The company is authorized to make such subdivisions, reclassifications, or consolidations of

such balances as are necessary to meet the requirements of this system of accounts.

21. Telephone plant acquired.—(A) When property in use in telephone service (note instruction 3-AA) is acquired, the amount of money actually paid (or the current money value of any consideration other than money exchanged) for the property (together with preliminary expenses incurred in connection with the acquisition) shall be charged to account 276, "Telephone plant acquired." (Note also account 139.)

(B) The accounting for the acquisition of the plant shall then be completed as follows:

(1) The original cost, estimated if not known, (Note instruction 3-S.1) of telephone plant, governmental franchises and other similar rights acquired shall be charged to the telephone plant accounts, account 100.2 "Telephone plant under construction", and account 100.3, "property held for future telephone use", as appropriate, and credited to account 276. When the actual original cost cannot be determined and estimates are used, the company shall be prepared to furnish this Commission with the particulars of such estimates.

(2) The amounts of the reserve requirements for depreciation and amortization of the plant acquired shall be credited to account 171, "Depreciation reserve", and account 172, "Amortization reserve", and debited to account 276.

(3) The amount of contributions to the predecessor company or companies for construction and acquisition of the telephone plant acquired shall be credited to account 175, "Contributions of telephone plant", and debited to account 276 on the books of the accounting company.

(4) The amount remaining in account 276, "Telephone plant acquired", applicable to the plant acquired, shall upon completion of the entries provided in the foregoing paragraphs (1), (2), and (3), be debited or credited, as appropriate, to account 100.4, "Telephone plant acquisition adjustment", except that when any amount thus chargeable to account 100.4, applies to duplicate or other telephone plant which will be retired by the vendee in the reconstruction of the acquired property and its consolidation with pre-

viously owned property, the accounting for the amount applicable to such plant shall be submitted to this Commission for consideration and approval.

[fol. 324] (C) Journal entries recording the acquisition of a complete telephone system, a complete exchange, a complete toll system, or other telephone plant where the consideration paid is $25,000 or more, shall be submitted to this Commission for consideration and approval. The text of such entries shall give a complete description of the property acquired and the bases upon which the amounts of the entries have been determined.

The defendant states that the foregoing parts of the Uniform System of Accounts and all the matters and things covered by the references therein are found in Exhibit B attached to the original Bill of Complaint.

The defendant, further answering paragraph 9 of the Bill of Complaint of the additional plaintiffs, states that the Uniform System of Accounts for Telephone Companies. Issue of June 19, 1935, is before the court in writing and that the meanin of account No. 100.4 and of account No. 100.1 is for the determination of the court upon examination of the text of the writing and that the requirements of said accounts as written therein are under the law subject to the ascertainment and declaration of the Federal Communications Commission in the administration of the Communications Act of 1934; and that if before the said Commission has had an opportunity to construe and apply said accounts the court takes jurisdiction to construe not only said accounts but the Uniform System of Accounts as set out in the Exhibit B attached to the original Bill of Complaint, the matter of construing the writing is then for the court and not for the additional plaintiffs.

The defendant states that it is without knowledge respecting the allegation that the additional plaintiffs acquired the greater part of their properties from other public utility companies and is without knowledge respecting the allegation that the greater part of their properties now existing have been recorded in said plaintiffs property investment accounts at actual cost to said plaintiffs whether in cash or securities.

The defendant denies that the requirements of Order No. 7-C of the Uniform System of Accounts are arbitrary or

[fol. 325] unreasonable or beyond the statutory power and authority of the Communications Commission; and the defendant denies that said requirements constitute an abuse of power and authority or an attempt to deprive the said plaintiffs of their property without due process of law; and the defendant denies that said requirements are illegal and void for reasons stated, or for any other reasons whatsoever.

a. The defendant, answering sub-paragraph a of paragraph 9 of the Bill of Complaint, states that it is without material facts; that it consists principally of conclusions; and that the plaintiffs are incompetent to declare the purpose of the Commission in making the requirements set forth in account No. 100.4(A), (B) and (C); but the defendant denies that the requirements respecting items of cost violate in any essential or vital respect the integrity of the account mentioned in said sub-paragraph a of paragraph 9 of the Bill of Complaint.

b. The defendant, answering sub-paragraph b of paragraph 9 of the Bill of Complaint of the additional plaintiffs, denies that the requirement that a portion of said plaintiffs' actual costs of property used in their business shall be carried in the plant acquisition adjustment account and that the items in such account shall be disposed of, written off or amortized in such manner as the Commission may direct, immediately and forthwith reduces, if it does not destroy, the value of items included in said account as assets on said plaintiffs' balance sheets; and the defendant denies that the requirement mentioned arouses suspicion as to the substantial character of the items in the said account; and the defendant denies that the segregation of costs into separate accounts gives any false or erroneous impression respecting the portion of the cost referable to account No. 100.4; furthermore, the defendant states that said sub-paragraph b of paragraph 9 states no cause of action or any part of a cause of action.

[fol. 326] c. The defendant, answering sub-paragraph c of paragraph 9 of the Bill of Complaint of the additional plaintiffs, alleges that the said plaintiffs are incompetent to declare the real purpose of the requirement mentioned in said sub-paragraph; that the said sub-paragraph does not state facts sufficient to constitute a cause of action or any part of a cause of action and that it ought to be

stricken from the Bill of Complaint; that what an analysis of account No. 100.4 will disclose is for the determination of the court upon an examination of the text of the requirement and not for the conclusion of the plaintiffs; and the defendant denies that the matter of prescribing account No. 100.4 as a part of the accounting system requires the plaintiffs to write off any portion of their actual investment or otherwise to dispose of it, but alleges that, on the other hand, the thing of which the plaintiffs complain is non-existent until some further order shall have been made by the Communications Commission with respect to the matter of writing off or amortizing investment or some part of it; and the defendant denies that the requirement of its classification of accounts is unauthorized, unreasonable and arbitrary.

d. The defendant, answering sub-paragraph d of paragraph 9 of the Bill of Complaint of the additional plaintiffs, alleges that it is argumentative and states conclusions and not facts; and the defendant alleges that Section 213(c) of the act is in nowise inconsistent with the requirements of said Order No. 7-C, and of said Uniform System of Accounts, Issue of June 19, 1935.

The defendant is without knowledge as to the allegation that the properties of the plaintiffs are composed for the most part of a large part of very small properties in rural communities previously owned by small local companies; and the defendant is without knowledge as to whether it will be impossible accurately to ascertain the actual money cost of these properties at the time when they were first dedicated to public use; but the defendant denies that estimates of original cost cannot be made with any degree of [fol. 327] accuracy.

The defendant denies that the inclusion of original cost in the balance sheets and account books of the additional plaintiffs will result in a misleading and inaccurate picture of said plaintiffs' true financial condition and history; and the defendant alleges that, on the contrary, such items will afford all persons a more accurate basis of information as to plaintiffs' true financial condition and history; and that placing items of original costs into balance sheets brings them out for public notice, whereas burying them somewhere else is inconsistent with the public interest.

The defendant denies that every legitimate purpose can be served by confining such figures of original cost to the statement provided for in Section 213 (c); and the defendant alleges that Section 213 (c), itself, anticipates that said data may be found from accounting records.

The defendant denies that any of the requirements for showing original cost, estimated if not known, in the accounts of plaintiffs are in anywise arbitrary or unreasonable.

e. The defendant, answering sub-paragraph e of paragraph 9 of the Bill of Complaint of the additional plaintiffs, denies that the requirements of the Uniform System of Accounts, Issue of June 19, 1935, prevents these plaintiffs from recording in their books and accounts any expense of depreciation which they may rightly incur; and respecting the fact that account No. 100.4 makes provision for amortization in some manner as the Commission may direct, the defendant states that the allowance of amortization over a definite period is practically the same as the allowance of depreciation and, that the alowance of amortization as provided for would take care of every legitimate right of the plaintiffs dependent upon the allowance of depreciation.

f. The defendant, answering sub-paragraph f of paragraph 9 of the Bill of Complaint of the additional plaintiffs, denies that the requirements of the Uniform System of Accounts, Issue of June 19, 1935, is impracticable of [fol. 328] application by said plaintiffs, and the defendant alleges that the plaintiffs have no right to complain in such manner until after they have made a bona fide effort to comply with Order No. 7-C and with the requirements of said System of Accounts; and furthermore, the defendant states that difficulty and expense supply no reason for refusal to make a bona fide effort to comply with said Order and said System of Accounts.

g. The defendant, answering sub-paragraph g of paragraph 9 of the Bill of Complaint of the additional plaintiffs, denies that the requirements of the Uniform System of Accounts, Issue of June 19, 1935, make radical changes in the completed accounts of said plaintiffs, although the said System may require a reclassification of items of account; and the defendant states that the matter of deter-

mining the power and authority of the Communications Commission under the Act of 1934 is a question of law for the court and not one of fact to be pleaded by the plaintiffs.

h. The defendant, answering sub-paragraph h of paragraph 9 of the Bill of Complaint of the additional plaintiffs, states that the ascertainment of the meaning of account No. 100.4 is a matter for the Federal Communications Commission under the Communications Act of 1934; that the bringing of this suit has prevented the said Commission from construing and applying said Account; that the text thereof is now in writing and before the court as it appears in Exhibit B attached to the Bill of Complaint of the original plaintiffs and that the matter of interpreting the said writing is now for the court and not for the plaintiffs; and the defendant alleges that said sub-paragraph h of said paragraph 9 states no cause of action or any part of a cause of action against this defendant and that the same should be eliminated from the Bill of Complaint; but the defendant denies that the authority of the Federal Communications Commission is limited to the making of [fol. 329] rules, regulations and classifications, and denies that it has no authority to issue an individual order requiring an individual carrier to make a specific accounting entry as it may direct with respect to matters under its jurisdiction and particularly with respect to matters coming under the accounting rules, regulations and classifications; and on this point the defendant states that Section 220 (g) of the Communications Act authorizes the defendant to approve accounts as well as to prescribe accounts; furthermore, the defendant alleges that Instruction No. 9 in the Uniform System of Accounts, Issue of June 19, 1935, provides as follows, to wit:

"To the end that uniformity of accounting may be maintained, the company shall submit all questions of doubtful interpretation of the prescribed accounting to this Commission for consideration and decision."

i. The defendant denies that the requirements of said System are inconsistent with and contrary to Sections 213 (c) and 219 (a) of said Act and Section 4 (i) thereof; and on the other hand, the defendant alleges that the Sections mentioned confer jurisdiction on the Federal Communica-

tions Commission which may be exercised in connection with the authority of said Commission under Section 220 of the Communications Act; and that authority under Section 213 (c) and under Section 219 (a) may be exercised at any time.

10. The defendant, answering paragraph 10 of the Bill of Complaint of the additional plaintiffs, states that the said plaintiffs have not considered the Uniform System of Accounts in its entirety and the defendant denies that the said System requires plaintiffs' accounts to show a liability for a contribution which the plaintiffs have not received; and that in this respect the System requires offsetting items which make the charge of which the plaintiffs complain proper and regular.

11. The defendant, answering paragraph 11 of the Bill of Complaint of the additional plaintiffs, alleges that said paragraph does not state any cause of action nor any part [fol. 330] of a cause of action; but the defendant denies that the dividing line between the classifications mentioned in said paragraph 11 are so indefinite and ambiguous as to be impossible for the understanding of the plaintiffs; and the defendant denies that the System of Accounts prescribed by the Communications Commission would require the plaintiffs to make entries in their accounts at their peril or at the risk of penalties prescribed by the Communications Act of 1934; and furthermore, the defendant states that where entries in the prescribed accounts are erroneously made in good faith, the penal provisions of the aforesaid Act do not apply.

12. The defendant, answering paragraph 12 of the Bill of Complaint of the additional plaintiffs, states that the account No. 100.3 therein mentioned is in its full text before the court being exemplified by Exhibit B attached to the Bill of Complaint of the original plaintiffs; that the construction and interpretation thereof would have been for the Communications Commission if the application of the Communications Act had not been intercepted by this suit and, that now and until the suit is determined the construction and interpretation of said account being in writing before the court is for the court and not for the plaintiffs; but the defendant denies that the account mentioned prevents the recording of depreciation expense with respect

to property under Account No. 100.3 for the time such property is included in said account or for any other time or under any other circumstances where the plaintiffs would be lawfully entitled to record the expense of depreciation; and the defendant denies that the requirements mentioned in paragraph 12 of said Bill of Complaint are contrary to fundamental principles of correct accounting and are arbitrary and unreasonable or are illegal and void.

13. The defendant admits that the Uniform System of Accounts requires that all charges to plant investment, in- [fol. 331] come, operating revenue and operating expense accounts shall be just and reasonable, and that any payments by plaintiffs in excess of just and reasonable charges respecting the matters mentioned shall be charged against income; but the defendant denies that such requirement is contrary to the fundamental principles of correct accounting, and denies that it is arbitrary and unreasonable; and the defendant denies that the plaintiffs would of necessity be required to make any charges, under the circumstances stated, at their peril or at the risk of penalties prescribed by the Communications Act; and the defendant denies that it is without authority to prescribe the requirement mentioned; but on the other hand, the defendant states that the requirement in the Uniform System of Accounts, whereby charges to investment and other accounts mentioned in paragraph 13 of the Bill of Complaint shall be just and reasonable, is valid; and, furthermore, the defendant alleges that all any carrier would of necessity be required to do in the premises to escape penalties under the law would be to make a bona fide effort to comply with the Communications Act and with the accounting requirements; and that under Section 220 (g) of the Act the Commission may approve, as well as prescribe, accounts, or the form of accounts, and that practice before the Interstate Commerce Commission respecting such matters became settled prior to the passage of the Communications Act of 1934; that accounting reports filed by carriers before the Interstate Commerce Commission have been, and are, there subjected to consideration and then to proper order, in all such matters, whether favorable or unfavorable to the carrier; that the said practice would prevail before the Federal Communications Commission; that no carrier attempting to comply with the accounting requirements prescribed by Order No.

7-C attacked in this suit could or would come under and be subjected to the penal provisions of the Communications Act until the rejection of its accounting report, when offered by [fol. 332] a carrier, and then not until the Commission in due course of business, might make and enter an order against the carrier specifying with respect to requirements in the particular instance and matter necessary to make the accounting report under consideration at the time conform to prescribed or approved accounting; and the defendant further states that under Instruction No. 9 in the accounting system heretofore mentioned no carrier could be subjected to the penal provisions of the law unless such carrier of its own will and accord should refuse to comply with the requirements of the Uniform System of Accounts, Issue of June 19, 1935; and furthermore, the defendant states that no carrier can be prosecuted by the Federal Communications Commission under the Communications Act without the authorization of the Attorney General and without the aid of some District Attorney.

14. The defendant, answering paragraph 14 of the Bill of Complaint of the additional plaintiffs, denies that the application of Order No. 7-C and the Uniform System of Accounts authorized thereby would result in the publication of financial statements radically different from what such statements ought to be in fact and in truth, and denies that the application of said Order and said System of Accounts would take the property of the plaintiffs without due process of law or in violation of constitutional provisions.

15. The defendant admits that the Issue of June 19, 1935; purports to constitute a complete system of accounts, but it denies that its provisions are interdependent and non-severable; and denies that the said Issue of June 19, 1935, and the said Order No. 7-C are illegal and void in their entirety upon the grounds alleged or upon any other ground.

16. The defendant admits that Order No. 7-C requires the additional plaintiffs during the year 1936 to keep the [fol. 333] system of accounts prescribed and admits that the Order requires the keeping of such portion or portions of accounts as kept under the present system, as may be necessary for comparison of 1936 results with the results

of previous years; but the defendant denies that this provision will affect so many of the accounts of the plaintiffs as to require any great expense; and furthermore, the defendant denies that the matter of expense supplies any reason for nullifying the Issue of June 19, 1935; and the defendant denies that the requirement mentioned in paragraph 16 of the Bill of Complaint is arbitrary and unreasonable, and denies that it is beyond the statutory power and authority of the Commission, and denies that it is illegal and void.

17. The defendant, answering paragraph 17 of the Bill of Complaint of the additional plaintiffs, states that the interpretation of the Order and the Uniform System of Accounts mentioned therein and the application thereof by further order is for the Federal Communications Commission, but this right on the part of the said Commission has been intercepted by this suit and that now the matter of interpretation during the pendency of the suit is for the court and not for the plaintiffs; that the said Order and the said Uniform System of Accounts are both in writing and are before the court as set out in Exhibit B attached to the Bill of Complaint of the original plaintiffs, but the defendant denies the effect and result of said Order and said System as alleged in paragraph 17 of said Bill of Complaint, and further pleading the defendant alleges that the plaintiffs have no right to prophesy what the Commission will finally require with respect to reporting under accounts Nos. 201, 100.1, 134.2 and 134.2(c) until the plaintiffs have made a bona fide effort to comply with the accounting system and shall have been damaged and injured by some order of the Commission hereafter made affecting accounting reports of the plaintiffs in connection with and with regard to the matters complained of in Section 17 of [fol. 334] the Bill of Complaint; and the defendant denies that the requirement mentioned in said section of the Bill of Complaint is contrary to established accounting practice and denies that it deprives any of the plaintiffs of its lawfully acquired corporate assets and denies that it confiscates property of any of the plaintiffs or that it is beyond the statutory powers of the Commission.

18. The defendant admits that Order No. 7-C and the Uniform System of Accounts, Issue of June 19, 1935, estab-

lish a separate expense account for maintenance expenses of classes of plant; and the defendant alleges that this is an improvement upon the first revised issue of the Interstate Commerce Commission currently in effect; that the requirement of accounts 602.1 to 602.9 will result in information which the Federal Communications Commission, as the regulating body or tribunal, very much needs; and the defendant alleges that the keeping of such accounts will result in economy by bringing to light facts and figures which ought to be known and understood by the Federal Communications Commission; and that such economy is much needed on behalf of the public interest; and the defendant denies that said Order No. 7-C and the Uniform System of Accounts provided thereby are arbitrary, unjust, unreasonable or contrary to law.

19. The defendant, further answering the Bill of Complaint of the additional plaintiffs, alleges that the Order of which the plaintiffs complain, was entered, as the date thereof indicates, on June 19, 1935; that the Uniform System of Accounts prescribed thereby was forthwith, and along with said Order, served on the additional plaintiffs; that thereafter the said plaintiffs took none of the steps and availed themselves of none of the procedure whereby pursuant to the Communications Act they might have brought any matter or thing of inaccuracy, inequity or invalidity to the attention of the Federal Communications Commission, to the end and for the purpose that any matter of inaccuracy, inequity or invalidity might be amended, corrected or otherwise modified or even annulled, rejected, [fol. 335] suspended and set aside; and furthermore, that without in the meanwhile giving the said Commission any opportunity to consider the things of which said plaintiffs complain in their Bill of Complaint, they waited to bring this suit for a period of 156 days, and until after a time when the Issue of June 19, 1935, could be modified so as to become effective on January 1, 1936; and the defendant states that after the issuance of Order No. 7-C and of the Uniform System of Accounts, Issue of June 19, 1935, the plaintiffs nelgected to move for a rehearing either before the Telephone Division of the Federal Communications Commission or by the Commission itself as they might have done under applicable provisions of the Communica-

tions Act, and as it was their duty to do before resorting to equity; and furthermore, the defendant states that after the effective date of the Issue of June 19, 1935, to wit, January 1, 1936, the plaintiffs might have, under the practice developed before the Interstate Commerce Commission under identical law, submitted their accounting reports at variance with the provisions of the accounting system and could have asked for approval under Section 220 (g) of the Communications Act giving reasons therefor both under said section and under Instruction No. 9 of the Uniform System, as well as under other provisions of existing law and upon the facts stated, the defendant pleads that the plaintiffs have been guilty of laches which ought to defeat their right to the relief and remedy for which they pray.

20. The defendant denies that under the Communications Act of 1934, and particularly under Sections 220, 501 and 502 thereof, the plaintiffs or any of them might be subjected to a multiplicity of suits and criminal prosecutions for the recovery and assessment of fines and penalties prescribed by said sections unless by preference they should invite such prosecutions and assessments because only wil- [fol. 336] ful violations of the Order and of the System of Accounts are denounced by law; and the defendant states that the plaintiffs are without reason to complain until they have made a bona fide effort to comply with the order and with the System of Accounts and until they have offered their accounting reports and have been subjected by the Federal Communications Commission to arbirtrary and unlawful orders respecting the same.

21. The defendant, answering paragraph 21 of the Bill of Complaint of the additional plaintiffs, states that the same is a matter of law and not a subject of proper pleading.

22. The defendant further answering the Bill of Complaint and without waiving its specific denials herein made, denies each and every allegation contained in said Bill of Complaint, excepting the matters and things heretofore specifically admitted, qualified or otherwise answered.

23. The defendant states there is no equity in the Bill of Complaint of the additional plaintiffs.

24. Wherefore, the defendant, Federal Communications Commission, prays that the said Bill of Complaint be dismissed, and that the defendant be discharged.

Federal Communications Commission, by (Sgd.) Hampson Gary, General Counsel. (Sgd.) Frank Roberson, Assistant General Counsel. (Sgd.) Albert E. Stephan, Assistant Counsel. (Sgd.) W. D. Humphrey, Assistant Counsel.

[fol. 337] *Duly sworn to by Paul A. Walker. Jurat omitted in printing.*

[fol. 338] IN UNITED STATES DISTRICT COURT

[Title omitted]

ANSWER OF THE FEDERAL COMMUNICATIONS COMMISSION TO THE BILL OF INTERVENTION OF EASTERN TELEPHONE AND TELEGRAPH COMPANY AND OTHERS, INTERVENING PLAINTIFFS—Filed December 23, 1935

Comes now the defendant, Federal Communications Commission, and answers the bill of intervention herein filed by the Eastern Telephone and Telegraph Company et al.

1. The defendant admits the incorporation and organization of the intervening plaintiffs as alleged in paragraph 1 of their bill of intervention.

2. The defendant, Federal Communications Commission, admits that it is an administrative tribunal, created by the Communications Act of 1934; that it is charged with the administration of said Act; and that it was organized on July 11, 1934, as alleged in paragraph 2 of the bill of intervention.

3. The defendant admits the allegations of paragraph 3 of the bill of intervention.

4. The defendant states that it is without knowledge of the matters and things set out in paragraph 4 of the bill of intervention and particularly that part of said paragraph 4 contained in the last subdivision thereof.

[fol. 339] 5. The defendant admits the facts and matters stated in paragraph 5 of the bill of intervention.

6. The defendant, answering paragraph 6 of the bill of intervention, states that it is without knowledge respect-

ing the operating revenues and the acquisitions of the intervening plaintiffs.

7. The defendant, answering paragraph 7 of the bill of intervention and noticing that it refers to and adopts sections numbered 6 to 16, inclusive, of the bill of complaint filed in this cause by the American Telephone and Telegraph Company et al., plaintiffs, now refers to and adopts as its answer to paragraph 7 of the bill of intervention the original answer of the defendant herein, wherein it answered the bill of complaint of the American Telephone and Telegraph Company et al., and the defendant adopts and pleads as fully as if set out herein at length as its answer to said paragraph 7 of the bill of intervention paragraphs 6, 7, 8, 9, 10, 11, 12, 13, 14, 15 and 16 of its said original answer to the bill of complaint of the American Telephone and Telegraph Company et al.; and the defendant refers to its answer herein filed to the bill of complaint of the Ohio Associated Telephone Company and others, additional plaintiffs, and adopts all pertinent parts of said answer and pleads the same in answer to the bill of intervention of the intervening plaintiffs.

8. The defendant, further pleading, refers to and adopts as a part of this answer, as fully as if set out at length herein, section numbered 18 of its answer filed herein to the bill of complaint of the American Telephone and Telegraph Company et al.

9. The defendant, answering further the bill of intervention denies each and every allegation therein contained, excepting the matters and things herein specifically admitted, qualified or otherwise answered.

10. The defendant states that there is no equity in the bill of intervention.

[fol. 340] Wherefore, the defendant prays that the bill of intervention be dismissed and that the defendant be discharged.

Federal Communications Commission, by (Sgd.) Hampson Gary, General Counsel. (Sgd.) Frank Roberson, Assistant General Counsel. (Sgd.) Albert E. Stephan, Assistant Counsel. (Sgd.) W. D. Humphrey, Assistant Counsel.

[fol. 341] *Duly sworn to by Paul A. Walker. Jurat omitted in printing.*

[fol. 342] IN UNITED STATES DISTRICT COURT

[Title omitted]

ANSWER OF UNITED STATES OF AMERICA TO BILL OF COMPLAINT OF AMERICAN TELEPHONE AND TELEGRAPH CO., ET AL.—Filed December 23, 1935

Comes now the United States of America, one of the defendants in the above entitled action and answering the bill of complaint filed herein by the American Telephone and Telegraph Company, et al., admits, denies and alleges in the manner following:

1. Defendant admits for the purposes of this suit that the facts alleged in Sections 1 to 5, inclusive, of plaintiffs' bill of complaint are true. Further answering Section 5 thereof, defendant states that on or about October 31, 1934 plaintiffs herein, acting pursuant to the permission extended in Orders Nos. 7 and 7-A of the Federal Communications Commission, filed with said Commission a lengthy statement in writing which set forth in detail their views respecting the proposed Uniform System of Accounts then under consideration by the Commission and bearing its Docket No. 2551; that on or about said date the National Association of Railroad and Utilities Commissioners, acting in behalf of the state regulatory commissions having supervision over telephone companies in 42 States of the Union, also filed a statement which set forth the views of [fol. 343] said commissions respecting said proposed Uniform System of Accounts; that while said matter was still pending before said Commission, additional statements bearing on said matter were filed by various other individuals, telephone associations, railroad and utility commissions; that each and all of said statements were carefully examined, studied and considered by said Commission and conferences were held with respect thereto prior to the issuance of said Commission's Order No. 7-B; that said Order No. 7-B, which was issued on May 1, 1935, set forth the proposed Uniform System of Accounts and notified all parties interested therein to file their exceptions thereto for consideration by the Commission at a conference to be held thereafter; that said conference was held on May 16 and 17, 1935, at which time plaintiffs and other interested

parties, appearing with attorneys, accountants and other representatives, submitted further statements in writing setting forth their objections and exceptions to said proposed Uniform System of Accounts; that on May 24, 1935, pursuant to the Commission's authorization plaintiffs and other interested parties filed with the Commission further statements in writing setting forth their views respecting said proposed System of Accounts; that each and all of the aforementioned statements were carefully examined, studied and considered by the Commission prior to the making of its Order No. 7-C.

2. Defendant denies each and every allegation contained in Section 6 of plaintiffs' bill and in connection therewith alleges that the Federal Communications Commission in issuing its Order No. 7-C and in respect of all other proceedings relating to said proposed Uniform System of Accounts then under its consideration was performing an administrative function of a legislative character authorized by Section 220 of the Communications Act of 1934, the exercise of which was made subject to Commission's discretion by Sub-division A of Section 220 of said Act; that the powers vested in said Commission under Section 220 of said Act [fol. 344] are not subject to and need not be exercised in accordance with the provisions of Section 404 or Section 213 of said Act; that Order No. 7-C, copy of which is annexed to plaintiffs' bill of complaint and marked Exhibit B thereof and which defendant admits to be a true copy thereof and adopts as part of this answer, in and of itself constitutes a report in respect of the Uniform System of Accounts and embodies a statement of the Commission's conclusions and its requirements in the premises.

3. Defendant admits the allegations contained in the first unnumbered paragraph of Section 7 of plaintiffs' bill respecting the requirements of the Uniform System of Accounts in the matter of recording "original cost" but in connection therewith defendant alleges that said Uniform System of Accounts in addition to requiring plaintiffs to record their properties upon their books of account at their "original cost" further requires in respect of said properties that they shall also record on the asset side of their balance sheet statement, in a separate account No. 100.4, the difference between the amount actually paid for

said properties and the original cost thereof diminished in each instance by certain specified charges; that said properties shall be treated further in said books of account in the manner more particularly set out in the Uniform System of Accounts which is hereby referred to for a complete enumeration of the requirements in respect to said matters.

4. Answering the second and succeeding unnumbered paragraphs of Section 7 of plaintiffs' bill, defendant states that it has no knowledge of the amount of property acquired by plaintiffs prior to January 1, 1913, or of the manner in which such properties have been recorded in plaintiffs' accounts, but, nevertheless, denies that the definition of "original cost" as contained in and read with the context of the Uniform System of Accounts will require plaintiffs in substance or in effect to so restate as of January 1, 1936, their property investment accounts by eliminating therefrom [fol. 345] their recorded cost or investment in property theretofore acquired by them from another public utility; defendant further denies that any property acquired by plaintiffs after July 1, 1936, shall be carried in their property investment account at an amount different from that which they may actually pay therefor; on the contrary, defendant alleges that the Uniform System of Accounts will require plaintiffs to keep a complete, accurate and intelligible record of all their property transactions. Defendant, answering further the unnumbered paragraphs of said Section 7 of plaintiffs' bill, denies that the Uniform System of Accounts would prevent plaintiffs from recording their proper expense of depreciation with respect to that portion of their property investment included in Account No. 100.4, or in any other account; and defendant alleges that plaintiffs' interpretations of said Uniform System of Accounts to contrary effect in respect of the foregoing matters is strained and unreasonable and not in accordance with Federal Communications Commission's interpretation thereof.

5. Defendant denies each and every allegation contained in paragraphs (a), (b) and (c) of Section 7 of plaintiffs' bill and further answering said paragraphs denies that the Uniform System of Accounts will require plaintiffs' property investment accounts to be kept on a basis which will reflect neither the fact of actual investment nor the value

thereof; or will conceal the amount of said actual investment or will substitute therefore the investment of some one else, or will conceal relevant facts, or misrepresent plaintifffffs' conditions, or will require plaintiffs to write off a part of their actual investments in any of the instances alleged, or will prevent plaintiffs from recording in their expense accounts the amount of depreciation actually incurred. Defendant alleges that the Uniform System of Accounts will require plaintiffs to keep their books of account in such a manner as will fully, accurately and clearly acquaint the Federal Communications Commission with the facts concerning plaintiffs' investments, which facts the [fol. 346] Commission is required to know for the purpose of performing the duties conferred upon it by the Communications Act of 1934; that said Uniform System of Accounts does not purport to change, alter or deny any property rights heretofore existing in favor of plaintiffs or any of them; that plaintiffs' interpretations of the terms of said Uniform System of Accounts to contrary effect in respect of the foregoing matters is strained and unreasonable and not in accordance with the Federal Communications Commission's interpretation thereof.

6. Defendant denies each and every allegation contained in paragraphs (d), (e), (f) and (g) of Section 7 of plaintiffs' bill, except it admits that the Uniform System of Accounts will require in many instances that plaintiffs' investment in a single item of purchased property be separated into two accounts, but denies that said requirement is arbitrary or unreasonable or that compliance therewith will be difficult or expensive. Defendant further alleges that with respect to the matters complained of in said paragraphs plaintiffs have placed a forced and unreasonable construction upon the provisions of the Uniform System of Accounts and upon the terms of the Communications Act of 1934; that the discretionary powers vested by Section 220 of said Act in the Federal Communications Commission in respect of prescribing Uniform System of Accounts for telephone companies is not limited or restricted by the provisions of Section 213 (c), 219 (a) or 4 (i) of said Act but is an additional and distinct administrative power conferred upon said Commission for the purpose of enabling it to perform more efficaciously and intelligently the several duties devolving upon it under said Act.

7. Defendant denies each and every allegation contained in Section 8 of plaintiffs' bill.

8. Defendant denies each and every allegation contained in Section 9 of plaintiffs' bill and in connection therewith alleges that there is no necessity or requirement that plaintiffs act at their peril in an endeavor to classify or charge their properties to the appropriate accounts provided in [fol. 347] said Uniform System of Accounts, but on the contrary alleges that adequate safeguards for the protection and guidance of plaintiffs have been provided in instruction No. 9 of said System of Accounts which specifically directs that all questions of doubtful interpretation as to the meaning of said System of Accounts shall be submitted to the Federal Communications Commission for consideration and determination.

9. Defendant denies each and every allegation contained in Section 10 of plaintiffs' bill and in connection therewith refers the Court to the Uniform System of Accounts (copy of which is annexed to plaintiffs' bill of complaint as Exhibit B thereof) for the full and complete text of Account No. 100.3 and requests that said account be construed and interpreted in the light of its direct language and in a manner consonant with the context thereof.

10. Defendant admits as alleged in Section 11 of plaintiffs' bill that the Uniform System of Accounts requires that all charges to plant investment, income, operating revenue and operating expense accounts shall be "just and reasonable" and that any payment by plaintiffs in excess of such just and reasonable charges shall be charged against income, but denies each and every remaining allegation contained in said Section 11. Defendant alleges further that instruction No. 9 of the Uniform System of Accounts in providing that all questions of doubtful interpretation concerning said System shall be submitted to the Federal Communications Commission adequately protects plaintiffs and establishes a mode of insuring them against any unwarranted exposure to peril or any involuntary risk of penalty of any kind under the Communications Act of 1934.

11. Defendant denies as alleged in Section 12 of plaintiff's bill that said Uniform System of Accounts will render it impossible for plaintiffs to keep accounts adequately for

any of the purposes enumerated therein; denies that it will require plaintiffs' accounts to conceal relevant facts or to misrepresent their condition to plaintiffs' damage; denies [fol. 348] that it will result in the publication of financial statements radically different from or contradictory to those heretofore issued by plaintiffs, unless, of course, such statements heretofore issued by plaintiffs have been false or fictitious; denies further that the requirements of said System of Accounts constitute a taking of plaintiffs' property without due process of law in violation of the Fifth Amendment to the Federal Constitution.

12. The defendant answering Section 13 of plaintiffs' bill denies that the provisions of the Uniform System of Accounts are so constituted that its provisions are interdependent and non-severable and denies further that Order No. 7-C and said Uniform System of Accounts are illegal or void either in whole or in part.

13. Defendant has no knowledge or information concerning the allegations of Section 14 of plaintiffs' bill relating to the amount of additional expense to which plaintiffs shall be put in complying with the terms of the Uniform System of Accounts and therefore defendant neither admits nor denies the same, but calls for strict proof thereof if the Court shall deem the same relevant and material. Defendant alleges that the validity of said System of Accounts is not to be determined by the amount of expenses involved in complying therewith and denies that the requirements complained of in said Section 14 are arbitrary or unreasonable or beyond the statutory power or authority of the Commission, or are illegal, or void, for these or any other reasons.

14. Defendant denies each and every allegation contained in Section 15 of the plaintiffs' bill and alleges further that the plaintiffs' have shown no basis for equitable relief herein.

15. Defendant admits, as alleged in Section 16 of plaintiffs' bill, that if plaintiffs do not comply with Order 7-C and keep the books of account therein prescribed by the Uniform System of Accounts on and after January 1, 1936, they shall be liable to the prosecutions, penalties and forfeitures provided in the Communications Act of 1934, but de-

fendant denies that plaintiffs shall be subject to any such [fol. 349] prosecutions, penalties or forfeitures or any multiplicity of suits for failing to do any of the several things which, as hereinabove indicated, plaintiffs have erroneously and unreasonably construed to be required of them by said Uniform System of Accounts.

16. Further answering plaintiffs' bill and the whole thereof, defendant denies each and every allegation contained therein except such as have been admitted or otherwise answered hereinabove.

Wherefore, having fully answered said bill of complaint, the United States of America prays that the relief asked by plaintiffs be denied and that the bill of complaint herein be dismissed with costs to plaintiffs, and that defendant have such other relief as may be just and proper.

Harold F. Collins, Special Assistant to the Attorney General. Lamar Hardy, United States Attorney, Southern District of New York.

Duly sworn to by Harold F. Collins. Jurat omitted in printing.

[fol. 350] IN UNITED STATES DISTRICT COURT

[Title omitted]

ANSWER OF THE UNITED STATES OF AMERICA TO BILL OF COMPLAINT OF OHIO ASSOCIATED TELEPHONE COMPANY, ET AL., ADDITIONAL PLAINTIFFS—Filed December 23, 1935

Comes now the United States of America, one of the defendants herein, and answering the bill of complaint filed by Ohio Associated Telephone Company, et al. admits, denies, and alleges in the manner following:

1. Defendant admits for the purposes of this suit that the facts alleged in Sections 1 to 7 inclusive of the bill of complaint of said additional plaintiffs are true.

2. Defendant further answering Section 6 of the bill states that on or about the dates on which exceptions and objections to the proposed System of Uniform Accounts were filed with the Federal Communications Commission

by the plaintiffs in the manner alleged in said Section 6 there were filed by numerous other interested parties additional statements respecting said matters; that all of said statements, including the exceptions and objections filed by these plaintiffs were discussed and considered at a conference held by the Commission on May 16 and 17, 1935, and thereafter were further studied and considered by the [fol. 351] Commission prior to the making of its Order No. 7-C.

3. Defendant answering Section 8 of the bill denies each and every allegation contained therein and in connection therewith alleges that the Federal Communications Commission in issuing its Order No. 7-C and in respect of all proceedings relating to said proposed Uniform System of Accounts then under its consideration was performing an administrative function of a legislative character authorized by Section 220 of the Communications Act of 1934, the exercise of which was made subject to said Commission's discretion by Subdivision (a) of Section 220 of said Act; that the powers vested in said Commission under Section 220 of said Act are not subject to and need not be exercised in accordance with the provisions of Section 404 of Section 213 of said Act; that Order No. 7-C, copy of which is attached as Exhibit B to the bill of complaint of the original plaintiffs herein and which defendant admits to be true copy thereof, and which it ac pts as part of this answer, in and of itself constitutes a report in respect of the Uniform System of Accounts and embodies a statement of the Commission's conclusions and its requirements in the premises.

4. Defendant admits the allegations contained in the first unnumbered paragraph of Section 9 of the bill which relates to the requirements of the Uniform System of Accounts in the matter of recording "original cost", but in connection therewith defendant alleges that said Uniform System of Accounts in addition to requiring plaintiffs to record their properties upon their books of account at their "original cost" further requires in respect of said properties that they shall also record on the asset side of their balance sheet statements, in a separate account No. 100.4, the difference between the amount actually paid for said properties and the original cost thereof, diminished in each

[fol. 352] instance by certain specified charges; that said properties shall be treated further in said books of account in the manner more particularly set out in said Uniform System of Accounts, which is hereby referred to for a complete enumeration of the requirements in respect of said matters.

5. Defendant answering the second and succeeding unnumbered paragraphs of Section 9 of the bill denies that Order No. 7-C and the Uniform System of Accounts require that plaintiffs shall record nothing in their accounts showing their proper expense of depreciation with respect to that portion of their property investment included in Account No. 100.4, or in any other account; defendant alleges further that plaintiffs' interpretations of said Uniform System of Accounts to contrary effect in respect of said matters is strained and unreasonable and not in accordance with the Federal Communications Commission's interpretations thereof. Defendant has no knowledge of the time, manner or amount of plaintiffs' property acquisitions but denies that Order No. 7-C and the Uniform System of Accounts in their application will *require plaintiffs to record* the same in their property investment accounts in any manner or form which is not complete, accurate, or intelligible. Defendant denies that the requirements of Order No. 7-C and the Uniform System of Accounts are arbitrary, unreasonable, or beyond the statutory power and authority of the Commission; that said requirements constitute an abuse of such power and authority, or an attempt to deprive plaintiffs of their property without due process of law in violation of the Fifth Amendment of the Constitution of the United States, or are illegal and void for the reasons enumerated in said Section 9, or for any other reason. Defendant alleges that plaintiffs' interpretations of said [fol. 353] Order No. 7-C and the Uniform System of Accounts to contrary effect are strained and unreasonable and not in accordance with the Commission's interpretations in respect of said matters.

6. Defendant answering paragraphs a, b and c of Section 9 of the bill denies the validity of plaintiffs' interpretations of the provisions of the Uniform System of Accounts set forth in said paragraphs, and alleges that said interpretations are strained and unreasonable and not in accordance

with the Federal Communications Commission's interpretations in respect of said matters. Defendant refers the Court to the Uniform System of Accounts for the full and authoritative text of all the account, including Account No. 100.4, and requests that the Court construe said Account in the light of the text and context thereof. Defendant denies that the Uniform System of Accounts in its requirements will violate the integrity of any of plaintiff's accounts in any essential or valid respect; or will cause a false or erroneous impression to be given concerning the cost of their investments or will reduce or destroy the value of items listed in any such accounts as physical assets on their balance sheets; or will compel plaintiffs to improperly write off or dispose of their actual investments. Defendant denies further that the requirements of the Uniform System of Accounts are unauthorized, unreasonable, or arbitrary in the particulars alleged or in any other respect.

7. Defendant answering paragraph (d) of Section 9 of the bill states that it has no knowledge or information concerning the alleged inaccuracy or incompleteness of the property account records of plaintiffs' predecessors but nevertheless it denies that it would be difficult or impossible [fol. 354] for plaintiffs to determine the "original cost" of its plant investments to the extent required by Account No. 100.4, which specifically authorizes "an estimate of any such cost" to be made in instances where the actual original cost is unknown. Defendant further denies that the determination of "original cost" in the manner prescribed by the Uniform System of Accounts will result in a misleading or inaccurate picture of plaintiffs' true financial condition and history, but alleges that said Uniform System of Accounts in its application will require a complete, accurate, and intelligible record to be made and kept in respect to such matters. Defendant denies that all legitimate purposes concerning the subject of original cost can be achieved by requiring plaintiffs to furnish a statement or report of the character contemplated by and provided for in Section 213 (c) of the Communications Act. Defendant denies the reasonableness and validity of the interpretations given by plaintiffs to the provisions of the said Act mentioned in Section 9 of the bill, and specifically denies that the discretionary power to prescribe Uniform Systems of Accounts for telephone companies, as vested in the Commis-

sion by Section 220 (a) of said Act is limited or restricted in any manner by the provisions of Section 213 (c) of said Act. Defendant alleges that the provisions of Section 220 of said Act, including Subdivision (a) thereof, constitute a separate and distinct grant of power by Congress to said Commission to be exercised "in its discretion" in order that said Commission may be thus enabled to perform more efficaciously and intelligently the several duties devolving upon it under said Act. Defendant denies that the requirements of the Uniform System of Accounts, particularly those respecting the recordation of "original cost" in a separate account on the asset side of plaintiffs' balance [fol. 355] sheets, are arbitrary or unreasonable, but alleges that they are fair, reasonable, necessary, and proper requirements within the competency of said Commission to prescribe in fulfilment of its duties under the Communications Act of 1934 and for the attainment of the objectives thereof.

8. Defendant answering paragraphs e, f, g, h, and i of Section 9 of the bill denies that the Uniform System of Accounts will prevent plaintiffs from recording in their expense accounts the expenses of depreciation actually incurred; or will add greatly to their accounting expenses; or will result in their accounts reflecting unreliable estimates in whole or in part; or will require radical or retroactive changes in completed accounts; or will enable the Commission arbitrarily and indiscriminately to require individual property acquisitions to be written off or otherwise disposed of. Defendant further denies that the requirements of said Uniform System of Accounts are inconsistent with or contrary to or violative of Sections 213 (c), 219 (a), or 4 (i) of said Communications Act of 1934, or that they bear no reasonable relation to the ends and purposes for which the Commission is authorized to prescribe Uniform Systems of Accounts. Defendant alleges that the discretionary power which is vested in said Commission by Section 220 (a) of said Act, empowering it to prescribe Uniform Systems of Account is not limited or restricted in any manner by the several other provisions of said Act referred to in Section 9 of the bill. Defendant alleges further that the full exercise of the discretionary powers conferred upon

the Commission by Section 220 of the Act, including Subdivision (a) of said Section, are essential to the fulfilment of the Commission's duties under said Act and are necessary to the attainment of the objectives of said Act.

[fol. 356] 9. Defendant denies each and every allegation contained in Section 10 of the bill and refers the Court to the Uniform System of Accounts and requests that said accounts be interpreted and construed in conformity with the language of the text and context thereof.

10. Defendant denies each and every allegation contained in Section 11 of the bill and in connection therewith alleges that there is no necessity or requirement that plaintiffs act at their peril in an endeavor to classify or charge their properties to the appropriate accounts provided in the Uniform System of Accounts but alleges that adequate safeguards for the protection and guidance of plaintiffs have been provided in Instruction No. 9 of said Uniform System of Accounts, that said Instruction 9 specifically directs that all questions of doubtful interpretation as to the meaning of said Uniform System of Accounts shall be submitted to the Commission for consideration and determination.

11. Defendant denies each and every allegation contained in Section 12 of the bill and in connection therewith refers the Court to the Uniform System of Accounts for the full and complete text of Account No. 100.3 and requests that said Account be construed and interpreted in conformity with the language of the text and context thereof.

12. Defendant admits as alleged in Section 13 of the bill that the Uniform System of Accounts requires that all charges to plant investment, income, operating revenue, and operating expense accounts shall be "just and reasonable" and that any payment by plaintiffs in excess of just and reasonable charges shall be charged against income, but denies each and every remaining allegation contained in said Section 13. Defendant alleges further that Instruction No. 9 of the Uniform System of Accounts in providing that all questions of a doubtful interpretation concerning said System shall be submitted to the Commission, adequately protects plaintiffs and establishes a mode of insuring them [fol. 357] against unwarranted exposure to peril or invol-

untary risk of penalty of any kind under the Communications Act of 1934.

13. Defendant denies as alleged in Section 14 of the bill that said Uniform System of Accounts will render it impossible for plaintiffs to keep accounts adequately for any of the purposes enumerated in said Section; or that it will require plaintiffs' accounts to conceal relevant facts or to misrepresent their condition to plaintiff's damage; or that it will result in the publication of financial statements radically different from or contradictory to those heretofore issued by plaintiffs, unless of course such statements heretofore issued by plaintiffs have been false or fictitious. Defendant denies further that the requirements of said Uniform System of Accounts constitute the taking of plaintiffs' property without due process of law in violation of the Fifth Amendment to the Constitution of the United States.

14. The defendant, answering Section 15 of the bill, denies that the provisions of the Uniform System of Accounts are so constituted that they are interdependent and nonseverable, and denies further that Order No. 7-C and said Uniform System of Accounts are illegal or void in whole or in part for the reasons alleged or for any other reason.

15. Defendant has no knowledge or information concerning the truth of the allegations of Section 16 of the bill which relate to the amount of additional expense to which plaintiffs shall be put in complying with the terms of the Uniform System of Accounts and, therefore, defendant neither admits nor denies the same but calls for strict proof thereof if the Court shall deem the same relevant and material. Defendant further alleges that the validity of said Uniform System of Accounts is not to be determined by the amount of expenses involved in complying therewith, and denies that the requirements complained of in said Sec- [fol. 358] tion 16 are arbitrary or unreasonable or beyond the statutory power or authority of the Commission or are illegal or void for these or any other reasons.

16. Defendant, answering Section 17 of the bill, denies that the requirements of Accounts 100.1, 134.2, or 201 of the Uniform System of Accounts are contrary to established accounting practices or that they deprive plaintiffs sev-

erally of their lawfully acquired corporate assets or that they confiscate plaintiffs' properties or exceed the statutory power of the Commission. Defendant refers the Court to the Uniform System of Accounts for the exact language of the above mentioned accounts and requests that they be construed and interpreted in conformity with the language of their text and context.

17. Defendant answering Section 18 of the bill denies that the requirements of Accounts 602.1 to 602.9 inclusive of the Uniform System of Accounts are arbitrary, unjust, or unreasonable, or that they place an unjust or illegal burden upon plaintiffs. Defendant directs attention to the fact that plaintiffs' bill of complaint herein does not allege sufficiently, or at all, that plaintiffs on and after January 1, 1936, will be required to establish and maintain accounts Nos. 602.1 to 602.9 inclusive of the Uniform System of Accounts; that it is alleged in Section 6 of the bill that the average annual operating revenues of each of the plaintiffs herein exceeds $50,000.00, but it is not alleged whether said revenues exceed $100,000.00. In this connection defendant directs attention to Instruction No. 1 (C) of the Uniform System of Accounts which provides that companies having average annual operating revenues exceeding $50,000.00, but not more than $100,000.00 may keep their accounts for operating revenues and operating expenses under the ac- [fol. 359] counts of the condensed classification provided for in said Uniform System of Accounts; that the mode of condensed classification prescribed for such companies is set forth in the right hand column on page 77 of the Uniform System of Accounts and there is eliminated therefrom accounts 602.1 to 602.9, the establishment and maintenance of which plaintiffs object to in their bill; that by reason of the facts aforesaid, plaintiffs have shown no cause for complaint in respect of the matters set forth in Section 18 of their bill.

18. Defendant denies each and every allegation contained in Section 19 of the bill and alleges that plaintiffs have shown no basis for equitable relief herein.

19. Defendant admits as alleged in Section 20 of the bill that if plaintiffs do not comply with Order No. 7-C and keep the books of account therein prescribed by the Uniform System of Accounts on and after January 1, 1936, they

shall be liable to the prosecutions, penalties, and forfeitures provided in the Communications Act of 1934, but defendant denies that plaintiffs shall be subject to such prosecutions, penalties, or forfeitures, or any multiplicity of suits for failing to do any of the several things which, as hereinabove indicated, plaintiffs have erroneously and unreasonably construed to be required of them by said Uniform System of Accounts.

20. Further answering plaintiffs' bill and the whole thereof, defendant denies each and every allegation contained therein except such as have been admitted or otherwise answered hereinabove.

Wherefore, having fully answered said bill of complaint, the United States of America prays that the relief sought by plaintiffs be denied and that the bill of complaint herein be dismissed with costs to plaintiffs and that defendants [fol. 360] have such othe relief as may be just and proper.

(Sgd.) Harold F. Collins, Special Assistant to the Attorney General. Lamar Hardy, United States Attorney, Southern District of New York.

[fol. 361] *Duly sworn to by Harold F. Collins. Jurat omitted in printing.*

[fol. 362] IN UNITED STATES DISTRICT COURT

[Title omitted]

ANSWER OF UNITED STATES OF AMERICA TO THE BILL OF INTERVENTION OF EASTERN TELEPHONE AND TELEGRAPH COMPANY, ET AL.—Filed December 23, 1935

Comes now the United States of America, one of the dedefendants in the above entitled action, and answering the bill of intervention filed herein by the Eastern Telephone and Telegraph Company, et al., admits, denies and alleges in the manner following:

1. Defendant admits for the purposes of this suit that the facts alleged in Sections 1 to 6, inclusive, of the bill of intervention are true.

2. Defendant in answer to Section 7 of the bill of intervention, which adopts Sections Nos. 6, 7 (with the exception

of the second paragraph thereof), 8, 9, 10, 11, 12 (with the exception of the second paragraph thereof) 13, 14, 15 and 16 of the bill of complaint filed herein by the American Telephone and Telegraph Company, et al., hereby refers to Sections 1 to 15, inclusive, of its answer to said bill of complaint and adopts each and all of said sections of said answer, the same as if they were set forth at length herein, as its answer to Section 7 of the bill of intervention herein.

[fol. 363] 3. Further answering the bill of intervention and the whole thereof, defendant denies each and every allegation contained therein except such as have been admitted or otherwise answered herein.

Wherefore, having fully answered said bill of intervention, the United States of America prays that the relief sought by intervening plaintiffs be denied and that the bill of intervention herein be dismissed with costs to the intervening plaintiffs, and that defendants have such other relief as may be just and proper.

(Sgd.) Harold F. Collins, Special Assistant to the Attorney General. Lamar Hardy, United States Attorney, Southern District of New York.

Duly sworn to by Harold F. Collins. Jurat omitted in printing.

[fol. 364] In United States District Court for the Southern District of New York

In Equity. No. 81-366

American Telephone and Telegraph Company, et al., Plaintiffs; Ohio Associated Telephone Company, et al., Additional Plaintiffs; Eastern Telephone and Telegraph Company, et al., Intervening Plaintiffs,

vs.

United States of America and Federal Communications Commission, Defendants; National Association of Railroad and Utilities Commissioners, Intervening Defendants.

Statement of Evidence under Equity Rule 75—Filed May 13, 1936

The above entitled cause came on to be heard on December 13 and 14, 1935, before a specially constituted District

Court convened pursuant to the provisions of the Urgent Deficiencies Appropriations Act, and consisting of the Honorable Martin T. Manton, C. J., the Honorable Augustus N. Hand, C. J., and the Honorable John C. Knox, D. J., upon plaintiffs', additional plaintiffs' and intervening plaintiffs' applications for a temporary restraining order and an interlocutory injunction.

[fol. 365] In support of said applications there was submitted and received, the following:

The affidavit of Andrew Sangster, verified on the 5th day of December, 1935; the affidavit of John T. Madden, verified on the 6th day of December, 1935; the affidavit of Roy B. Kester, verified on the 6th day of December, 1935; the affidavit of B. F. Young, verified on the 6th day of December, 1935; the affidavit of Charles A. Heiss, together with Appendix A and Appendix B thereunto annexed, verified on the 6th day of December, 1935, all filed herein on the 12th day of December, 1935; and the affidavit of Harold V. Bozell, verified on the 6th day of December, 1935 and filed herein on the 10th day of December, 1935. Said affidavits respectively are as follows:

[fol. 366] [Title omitted]

AFFIDAVIT OF ANDREW SANGSTER

STATE OF NEW YORK,
County of New York, ss:

Andrew Sangster, being duly sworn on oath, deposes and says:

I reside at Chatham, New Jersey and am a consulting accountant with offices in the City of New York. For the last twenty years I have been practising in that profession, specializing in matters pertaining to public utility accounting, in which capacity I have been employed by State Public Utilities Commissions, Municipalities, and Public Utility Corporation to advise and assist in public utility valuations [fol. 367] and rate cases, and to perform accounting services in connection therewith. In the general practice of my profession I have been employed by the War Department of the United States Government and by the Federal Trade Commission.

In connection with valuations and rate cases relating to telephone companies I have investigated the accounts of the

New York Telephone Company, the New Jersey Bell Telephone Company, the Illinois Bell Telephone Company, The Chesapeake and Potomac Telephone Company (District of Columbia), The Chesapeake and Potomac Telephone Company of Baltimore City, The Chesapeake and Potomac Telephone Company of Virginia, the Southern Bell Telephone and Telegraph Company, and the Cumberland Telephone and Telegraph Company, and have performed accounting services in the same connection for various smaller telephone companies.

I have examined the Uniform System of Accounts for Telephone Companies prescribed by the Federal Communications Commission under the provisions of the Communications Act of 1934, Issue of June 19, 1935, effective January 1, 1936, and have considered the effect of the requirements of said system of accounts viewing those requirements from the standpoint of fundamentally sound and [fol. 368] correct accounting principles. With respect to certain of those requirements I believe and here affirm that they are contrary to the said accounting principles and to proper accounting methods; the particular requirements referred to and the respects in which they severally depart from the aforementioned principles and methods are set forth in the following statement.

I. Plant and Property Accounts

"Original Cost".—In the series of accounts prescribed by the Commission as those which will function as balance sheet accounts of telephone companies, five separate accounts are provided (in the group "I Investments") for the purpose of recording expenditures and retirements relating to plant and property:

100.1 Telephone plant in service.
100.2 Telephone plant under construction.
100.3 Property held for future telephone use.
100.4 Telephone plant acquisition adjustment.

* * * * * * *

103 Miscellaneous physical property.

The first of those accounts embraces a subordinate series numbered 201 to 277 inclusive, which are desinated "tele-

phone plant accounts." In the practical application of the system with respect to accounts 100.2 and 100.3, a corresponding subdivision would also be necessary, in fact the text of the latter account specifically provides for such a [fol. 369] subordinate series with a distinguishing prefix, but there is an important difference between this last mentioned series and the "telephone plant accounts" regarding their relation to depreciation accounting as will be stated hereinafter.

In the text pertaining to those three plant accounts (pages 26 and 27) it is provided that account 100.1 shall include "the original cost (note instruction 3-S.1) of the Company's property used in telephone service * * *"; account 100.2 shall include "the original cost (note instruction 3-S.1) of construction of telephone plant not completed ready for service * * *"; account 100.3 shall include "the original cost (note instruction 3-S.1) of property owned and held for imminent use in telephone service under a definite plan for such use." Instruction 3-S.1 (at page 5) defines the term "original cost" as follows:

"Original cost" or "cost", as applied to telephone plant, franchises, patent rights, and right of way, means the actual money cost of (or the current money value of any consideration other than money exchanged for) property at the time when it was first dedicated to the public use, whether by the accounting company or by a predecessor public utility. (Note also instruction 3-G.1)"

Referring to instruction 3-G.1 it is apparent that this definition applies solely and exclusively to telephone plant, [fol. 370] franchises, patent rights, and right of way. Instruction 3-G.1 (at page 4) states:

" 'Cost', except as applied to telephone plant, franchises, patent rights, and right of way, means the amount of money actually paid (or the current money value of any consideration other than money exchanged) for property or services. (Note also Instruction 3-S.1.)"

The practical effect of this definition of original cost in all transactions involving the purchase by the accounting company of property already devoted to the public use is that accounts 100.1, 100.2, and 100.3 will not show the actual money cost to the accounting company of such property,

unless by coincidence the actual cost is exactly the same as the "original cost", as the latter is defined in instruction 3-S.1. And since those three accounts must include only "original cost", estimated if not known (instruction 21), the definition necessarily applies retroactively.

To absorb the differences, plus or minus, between (a) actual cost plus expense of acquisition and (b) the so-called original cost of purchased property less reserve requirements for depreciation, the Commission has provided an account entitled "100.4 Telephone plant acquisition adjustment", the fourth account referred to by affiant on page 3 above. The full text pertaining to this account is contained on pages 27 and 28 of the system of accounts; paragraph C [fol. 371] provides for the disposition of the amounts therein recorded in the following manner:

"(C) The amounts recorded in this account with respect to each property acquisition shall be disposed of, written off, or provision shall be made for the amortization thereof in such manner as this Commission may direct. (Note also instruction 21.)"

No further provisions are to be found elsewhere in the system of accounts whereby the accounting company is informed definitely or at all as to what accounts are to be charged when stated amounts are directed to be disposed of, written off, or amortized—whether they shall finally be charged to operating expenses, or be treated as deductions from income or surplus. One certainty concerning said amounts is that they are rigidly and entirely excluded from the formal routine prescribed for depreciation accounting; under the rules prescribed by the Commission the classes of plant with respect to which depreciation charges may be accrued by the accounting company, "and the accounts covering such plant", are confined to those included in "telephone plant accounts", i. e., the depreciable accounts in the series numbered 201 to 277 inclusive, comprising the subdivision of "100.1 Telephone plant in service." Instruction 82 (page 24 of system of accounts) unequivocally so provides.

[fol. 372] It is evident that all of the foregoing accounting structures, with its peculiar effects upon the accounting company, is predicated upon the Commission's definition of "original cost." There is no recognized definition of

original cost known to this affiant other than that indicated or implied by the use of the term in the uniform system of accounts for telephone companies prescribed by the Interstate Commerce Commission, and the definition contained in the uniform systems of accounts for gas and electric companies adopted by the National Association of Railway and Utilities Commissioners (approved November 1922 and currently in effect). Original cost in all those systems of accounts means actual money cost to the accounting company, i. e., cost of material, labor, supplies, and other elements of direct cost, and a proper proportion of indirect costs or overhead charges determined upon some factual basis. Amounts charged to plant accounts must be the actual cost of the property acquired at the time of its acquisition.

The effect of the rules prescribed by the Commission in its system of accounts is that none of the three accounts "100.1 Telephone plant in service", "100.2 Telephone plant under construction", and "100.3 Property held for future telephone use" will show the actual money cost to the ac- [fol. 373] counting company of the property included in those accounts where the property has been purchased from another utility at a cost different from the cost to the original utility. The so-called telephone plant accounts included under account 100.1 will be subject to the same impairment by the application of those rules. Said rules require that the actual cost of property purchased by the carrier from another utility shall be charged in part to one or other of the three accounts above mentioned and in part to account "100.4 Telephone plant acquisition adjustment." But, as previously noted, the amounts standing in account 100.4 are subject to the arbitrary rule that they shall be disposed of as directed by the Commission in some manner unknown to the accounting company.

It is axiomatic in sound accounting principles that the accounts of a public utility company should be kept so that they shall show the actual cost of construction or acquisition, as well as the actual revenues and expenses received and incurred in the conduct of the business at or for any stated time. Only upon that basis can a balance sheet prepared from those accounts truly and accurately reflect the financial position of the company; however, there is one well recognized qualification to the actual cost principle,

[fol. 374] obviously sound, viz: that inventories and securities owned should be stated either at cost, or at market value or cost whichever is lower, the basis being definitely indicated. Accounts kept on such basis as that required by the system of accounts prescribed by the Commission would not truly reflect the financial position of the company, its balance-sheet and operating statements would be misleading if relied upon by legislators, courts, and taxing and other authorities, or by investors and the public generally. In particular the balance sheet would show (as it must) an account designated "100.4 Telephone plant acquisition adjustment" which, to the minds of most persons reading the same, would be either unintelligible or would convey the impression that it represented an asset of dubious character. Furthermore, were a competent practising accountant called upon to certify such balance sheet containing a relatively substantial amount in said account it would be his duty, In the opinion of this affiant, under the circumstances surrounding the status of that account, to require that a reserve of equivalent amount be created out of surplus or otherwise as protection against possible extinction of the asset. In the event that compliance with such requirement was refused it would be the duty of said accountant to so qualify his certificate on the aforesaid balance [fol. 375] sheet that the account in question would be characterized as an investment of no material value.

Viewing all these distorted effects produced by the sytem of accounts prescribed by the Commission with respect to plant and property accounts it is evident that the definition of original cost contained in said system of accounts is manifestly unsound and incorrect; such definition as applied in said system of accounts leads to results which would be in direct conflict with universally recognized and accepted accounting principles.

Depreciation.—In the system of accounts prescribed by the Commission the rules governing the accounting for depreciation are contained in instructions 80, 81, 82, and 83 (at pages 22-24) and in the text of the accounts provided for depreciation expense and depreciation reserve, (at pages 44 and 90).

The method of computation of depreciation rates is stated in instruction 80(A) which requires first:

"Depreciation charges shall be computed by applying the composite annual percentage rates considered applicable to the original cost (note instruction 3-S.1) of each class of depreciable telephone plant owned or used by the company * * *."

The classes of "depreciable telephone plant" are specified under instruction 82 as those covered by the depreciable accounts included in telephone plant accounts 207 to 264 [fols. 376-378] which, as previously noted, are a series of subordinate classifications included in account "100.1 Telephone plant in service."

[fol. 379] Since depreciation charges and accruals are permitted only with respect to "original cost" (as defined by the Commission) it necessarily follows that the amounts included in account "100.4 Telephone plant acquisition adjustment" are entirely excluded from the Commission's definition of depreciable property, notwithstanding that said amounts represent a portion of the actual cost of acquisition of depreciable property purchased by the accounting company. In place of adequate reimbursement to the company through proper depreciation charges and accruals, regularly made in accordance with recognized accounting rules, the amounts required by the Commission to be included in the aforesaid account are subject to the mandatory provision that they must be disposed of, written off, or amortized in whatever manner the Commission may direct. Thus, while the company is prevented from protecting itself against ultimate and inevitable loss by making normal and reasonable charges to operating expenses to provide against such depreciation, it may, at any time, be required to wipe out the said amounts as an investment loss which, in reality, it has not sustained.

[fol. 380] It is apparent from the foregoing examination and analysis that the rules prescribed in the instructions for depreciation accounting do not, in the instances cited, adequately provide against loss of service value certain to be realized when the property in question is finally retired from service. Said provisions are inaccurate, unreliable, and unsound, and therefore contrary to the fundamental principles of accounting.

* * * * * * *

[fol. 381] III. Distinctions as to Classification of Plant

The text of account "100.1 Telephone plant in service" states that it shall include the original cost of the company's property used in telephone service. Account "100.3 Property held for future telephone use" states that it shall include the original cost of "property owned and held for imminent use in telephone service under a definite plan for [fol. 382] such use." Account "103 Miscellaneous physical property" includes the investment in physical property other than the property to be classified under accounts 100.1, 100.2, and 100.3.

To observe the aforesaid rules and make them effective it would be necessary for the accounting company to know, through its responsible officers, what is the practical meaning of the terms "property used in telephone service" and "property held for imminent use" and where the line of demarcation should be drawn between them. The Commission having laid down no definition of either term which can be put into practical effect, great difficulty will inevitably be experienced by the accountants in attempting to make the required distinction. The same difficulties will confront them in attempting to distinguish between plant in use or held for imminent use and plant which, under the Commission rules, should be charged to account "103 Miscellaneous physical property."

As to the first distinction it is frequently stated by witnesses for telephone companies that certain portions of the plant and property consist of spare facilities, which means that such items as central office switchboards, ducts in underground conduit, cable, and so on have a capacity greater [fol. 383] than the use actually being made of them; when such capacity is functionally realized new units must be installed with sufficient capacity to care for expected growth over a period of time. I am informed that, in dealing with instances of that kind, accountants for regulatory bodies have contended that only part of the switchboard, conduit or cable, as the case may be, is "used in telephone service." A further refinement would be required in dealing with plant temporarily out of service. Telephone companies' monthly reports and statistics show that subscribers' circuits in cables are going in and out of service continuously with the installation and removal of telephones.

Regarding the distinction between miscellaneous physical property and telephone plant, questions would certainly arise in the familiar case where land is acquired, the area being greater than that necessary for immediate use because of a prudent provision for future growth. The investment for future needs might be classified in either of the accounts 100.3 and 10.3 depending upon the views of the individual making the distinction.

In the absence of practical and adequate definitions of the terms used in the instructions prescribed by the Com- [fol. 384] mission it is apparent that through the inevitable conflict of opinion which will arise, certain confusion and lack of uniformity will result from any attempt to faithfully observe the instructions as they appear in the system of accounts. This is contrary to sound accounting practice and therefore subversive of recognized accounting principles. In the Interstate Commerce Commission uniform system of accounts, first revised issue, all telephone plant was carried in the single balance sheet account "Telephone plant", thus avoiding such impractical distinctions.

IV. Just and Reasonable Charges

Under instruction (2-B.1) of the system of accounts it is required that all charges to accounts prescribed for telephone plant, income, operating revenues, and operating expenses shall be just and reasonable, and that any payments by the company in excess of such just and reasonable charges shall be charged against income. So far as this affiant can find from an examination of the system of accounts there is no basis of procedure set forth therein which would indicate and determine what steps are necessary to comply with said requirements. Before actually recording the facts relating to all transactions accounting officers would have to inform themselves as to what is or is not reasonable under the requirements of the system of ac- [fol. 385] counts. This is impractical and impossible under the circumstances. In any event the function of the accounts is to record the actual facts of the transactions in the orderly course of the company's affairs.

V. Necessity for Accurate Accounting

Under all circumstances accounts must accurately record the facts of a company's transactions and truly reflect its

actual condition for the information of the management, so that the business may be intelligently and effectively managed, accurate reports made to various taxing and governmental authorities, and true and complete statements prepared for the information of stockholders and prospective investors. The uniform system of accounts for telephone companies, first revised issue, prescribed by the Interstate Commerce Commission is, in my judgment, a system of accounts which is adequate for the aforesaid purposes and, on the whole, is based upon sound principles of accounting. The uniform system of accounts, "issue of June 19, 1935" prescribed by the Federal Communications Commission is, in my judgment, inadequate for the aforesaid purposes; it would be in part misleading since it would in certain respects distort relevant facts as hereinbefore [fol. 386] set forth, and hence is contrary to sound principles of accounting in said respects.

VI. Unsound Provisions Not Severable

The uniform system of accounts, issue of June 19, 1935 purports to be an essentially complete and integrated system of accounts. If the provisions hereinabove set forth and characterized as unsound or inaccurate and hence contrary to the fundamental principles of correct accounting were rendered void and without effect the system would no longer preserve its integral character. Vital and important parts necessary to a complete system of accounts would be defunct and unless new provisions were substituted therefor it would be impossible to keep adequate accounts in accordance with such system.

(Sgd.) Andrew Sangster.

Subscribed and sworn to before me this 5th day of December, 1935. (Sgd.) Charles M. Deal, Notary Public. Notary Public, Kings Co., No. 363, Reg. No. 7148. Cert. Filed in N. Y. Co. No. 393, Reg. No. 7-D-225. Commission Expires March 30, 1937. (Seal Charles M. Deal, Notary Public, Kings County.)

[fol. 387] [Title omitted]

AFFIDAVIT OF JOHN T. MADDEN

STATE OF NEW YORK,
County of New York, ss:

John T. Madden, being duly sworn on oath, deposes and says:

I reside at 710 Berkeley Avenue, Orange, New Jersey. I am Dean of the School of Commerce, Accounts, and Finance of New York University, and have served in this capacity since 1925. I have taught accounting in the University since 1911, and have served as Professor of Accounting since 1917. I am a Certified Public Accountant, licensed in [fol. 388] the States of New York and New Jersey. I am a past president of the American Association of University Instructors in Accounting, and a past president of the American Association of Collegiate Schools of Business. I have been engaged continuously in the practice of accountancy in New York City since 1911, as an associate of Leslie Banks and Company, 1910 to 1912; on my own account from 1912 to 1916; as partner in the firm of Madden and Reass from 1916 to 1922; and since 1922 have practiced as a consultant on special cases only. I have had considerable experience in the accounts of gas and electric utilities.

I am a member of the following professional associations among others:

New York State Society of Certified Public Accountants, (former director).
New Jersey Association of Certified Public Accountants.
American Society of Certified Public Accountants.
American Institute of Accountants.
National Association of Cost Accountants.

I actively participated in the technical programs of two international congresses in Accounting, one at Amsterdam, Holland, in 1926 and the other in New York, in 1929.

I am author of several works on accounting and have written articles or made addresses on the subject at various times and places.

[fol. 389] I have examined the uniform system of accounts for Telephone Companies prescribed by the Federal Communications Commission, Issue of June 19, 1935.

I. Original Cost Requirements

The new system of accounts provides two definitions of "*cost*". "Original Cost" or "Cost," as applied to telephone plant, franchises, patent rights, and right of way means the actual money cost (or equivalent) of property at the time when it was first dedicated to the public use, whether by the accounting company or by a predecessor utility (Instruction 3-S. 1—p. 5 of System of Accounts).

Cost, except as applied to telephone plant, franchises, patent rights, and right of way means the amount of money actually paid (or equivalent) for property or services. (Instruction 3-G. 1-p. 4).

Among the investment accounts the four here relevant are as follows:

100.1 Telephone plant in service
100.2 Telephone plant under construction
100.3 Property held for future telephone use
100.4 Telephone plant acquisition adjustment.

Disregarding for the moment, depreciation, amortization, and contributions, the new system requires that the ac- [fol. 390] counting company shall reclassify existing property investment accounts, for property purchased by it in the past, and after ascertaining or estimating the original cost of the property when first dedicated to public use by the predecessor company, enter such original cost in one or more of the first three mentioned property accounts. Future purchases of property from another utility are to be treated in the same manner.

If the purchase price or investment cost actually paid by the accounting company is greater or less than the original cost to the predecessor company when first dedicated to the public use, the difference is to be entered in account 100.4, Telephone plant acquisition adjustment. If, by coincidence, the accounting company happened to pay the seller exactly what the property originally cost the first dedicator to public use, no entries would be necessary in this account (pp. 25, 26, 27).

Provision is made by the new system for depreciation on the purchase or investment cost of the items included in the first mentioned account, 100.1. On the other hand, those items that represent investment cost but which must

be segregated in account 100.4, Telephone plant acquisition adjustment, are not included in the list of classes of [fol. 391] depreciable telephone plant (Instruction 82, p. 24). Instead, the new system provides that the items of investment cost which are segregated in account 100.4 "*shall* be disposed of, written off or provision made for the amortization thereof in such manner as the Commission may direct." (Vide Instruction 21, p. 12; also, paragraph C, top p. 28.)

Effect of These Requirements

The effect of these requirements is that where property has been purchased from some other utility at prices different from the original cost to the former owner, the purchaser or accounting company must ascertain if possible, (or if not possible, estimate) the original cost of such property to the former owner and enter these in accounts 100.1, 100.2 and 100.3, while the difference must be debited or credited to account 100.4. In other words, the investment cost or acquisition cost of the accounting company is not distributed by classes of property over the accounts 100.1, Telephone plant in Service; 100.2, Telephone Plant under construction; 100.3, Property Held for Future Telephone Use, but over four accounts, the first three of which represent the investment of a former owner, while the fourth account, 100.4, Telephone Plant Asquisition Adjustment, [fol. 392] is debited or credited with the difference, and it is this amount which must be extinguished, either proximately or remotely, at the sole pleasure of the Commission.

Reasons Why These Requirements are Contrary to the Fundamental Principles of Correct Accounting

It is universally recognized that correct accounting requires that a company's accounts shall record the transactions of that company and shall truly reflect its own actual costs.

When property is purchased, correct accounting requires that the agreed price at which the vendor parted with the property, (plus incidental costs of acquisition) shall be recorded as the vendee's investment or cost.

It is unsound and incorrect to keep a company's accounts neither on the basis of cost to it, nor of value, but on the basis of the cost of another or former owner.

The investment which owners have made in their property is a relevant fact which the accounts must correctly disclose, and any system which by direction or implication conceals such relevant fact is unsound in accounting, and misleading to all persons, including public bodies, who have occasion to rely on the accounts.

[fol. 393] While the balance in account 100.4, Telephone Plant Acquisition Adjustment, is listed as an investment asset (p. 25), the extingiushment of the balance is mandatory (Account 100.4 C, p. 28), and may be proximate or remote as the Commission may direct. Under the circumstances, the inclusion of this amount under the heading of "Investment" in the Balance Sheet may be misleading to an investor who does not acquaint himself with the requirements of the new system. The use of the word "adjustment" may connote the ephermeral character of the item to an experienced analyst or accountant but, under the circumstances, its inclusion among sound investments when there is the possibility that the Commission may order it to be written off forthwith, violates all ethical and moral principles of statement presentation. A sound investment should not be thus labeled.

In truth, the balance shown under account 100.4, under the new system is a deferred charge, since the Commission may make it so at any time. Because of this uncertainty, it is for all practical purposes an offset against surplus. A balance sheet which would fail to call specific attention on its face to the fact that the Commission must extinguish this item and may extinguish it immediately by a write-off is incomplete and misleading, and not in accord with correct accounting principles.

[fol. 394] Accounts should reflect transactions that have taken place as they take place. The cost of property to some former owner may be interesting and valuable statistical information, but it has no place in the accounts of the present owner, and any device which attempts to set forth, as accounting facts, things other than those which have actually taken place is incorrect and unsound.

Values to a former owner may be different from those envisioned by a new purchaser. Thus a present owner of land with a building upon it, places a value on both his land and his building. A prospective purchaser who desires this particular plot may value the property as a site for a new

building, in which instance the existing building would be, from his point of view, an actual encumberance, because he must necessarily remove it. Hence, the new owner will value the property when acquired solely as the value of land. This sound principle is recognized in the new system of accounts on future acquisitions of land with buildings thereon (See account 211, B, p. 49). The same philosophy of accounts applies in the purchase of any property. The vendee acquires property at a price which represents his investment and his determination of value, both in the ag- [fol. 395] gregate and in the components, regardless of the former owner's costs or concept of value.

Moreover, the new system, in providing such an arbitrary and unsound procedure, overlooks the fact that the book costs of the predecessor may not be kept on sound principles, and takes no account of differences in price levels since the predecessor acquired his property.

The investment which an owner makes in property is the actual cost of the property. The amount required to be charged in Account 100.4 must be written off at the discretion of the Commission. The accounting company is not permitted to show its own valuation (as measured by the price it paid) of property which it purchased, but must show the prior owner's original cost. If the Commission should order, as in its sole discretion it may, that Account 100.4 be written off more rapidly than the actual depreciation in the property through service, the accounts will nowhere reflect the true amount of the owner's investment. A loss which has not actually occurred will be recorded, which is contrary to all recognized principles of correct accounting. The definition of original cost as set forth in the new system is not supported by any authority on accounting. [fols. 396 & 397] Nor is there any persuasive argument that can be advanced to adopt a new method of accounting practice so contrary to universally accepted practice and so arbitrary in its requirements.

I express no opinion as to whether, for purposes of valuation in rate cases, the "original cost" as defined by the Commission, would be useful information, but it is my considered opinion that keeping accounts on this basis would be futile for any other purpose which accounting records should serve.

* * * * * * *

[fol. 398] III. Requirements of New System With Respect to Telephone Plant in Service, Property Held for Future Telephone Use, and Miscellaneous Physical Property.

The new system of accounts requires that the "original cost" of a company's physical property, (see discussion under title I above) except telephone plant under construction, shall be recorded in one of three accounts, viz., account 100.1, Telephone plant in service, account 100.3, Property held for future telephone use, and account 103, Miscellaneous physical property.

Under the regulations, the first mentioned account shall include plant "used" in telephone service at the date of the balance sheet. The second account above mentioned includes "property owned and held for imminent use in telephone service under a definite plan for such use." The last named account includes all other physical property.

I am informed that a large part of the total property in the telephone business consists of large units, such as a cable, which in turn consists of many pairs of fine wires, a part of which only may be in use at a given time. I am also informed that in such a case it has been contended by accountants for some regulatory bodies that since a part only of the wires in the cable are in use, therefore a part only of the cable is "used" in telephone service; while the com-
[fol. 399] panies, on the other hand, contend that when some wires in a cable are in use the cable itself is "used". I am further informed that small items of telephone plant, such as a pair of wires in a cable or a circuit in a switchboard continually go in and out of service as telephones are installed or removed, or as plant goes out of order temporarily and as traffic ebbs and flows. An accountant who attempts honestly to carry out the letter of these regulations is first confronted with the difficulty of deciding whether the use of property is imminent. The word has no particular significance in so far as accounting terminology is concerned, and the word might mean one thing to one and another thing to another accountant charged with making the record of the same transactions. Imminent might connote to one within a few weeks, say a month or two, or to another a longer period of time. Furthermore, on the basis of the information furnished me, as above stated, the practical difficulties which would be encountered

in attempting to draw the line of demarcation between property "used in telephone service" and property held for imminent use, without a more definite guide, would be insuperable.

[fols. 400-405] The definitions are too vague to guide accountants in determining what property to charge to accounts 100.1, 100.3, and 103. Such definitions are destructive of uniformity in account keeping. Furthermore, the words "used in telephone service" and "held for imminent use" put an intolerable burden upon the accountant who has such a vague definition to control his decision as to which plant account should be charged. Unless more precise definitions are adopted there will be an impairment in the usefulness of the uniform system for administrative and other purposes.

* * * * * * *

[fol. 406] V. Just and Reasonable Charges

The new system of accounts requires that all charges to plant investment, income, operating revenue and operating expense accounts shall be just and reasonable (Instruction 2 B-1, page 2) and that any payments by the company in excess of such just and reasonable charges shall be charged against income. The determination of what are just and reasonable charges must be a matter of judgment to a considerable extent by the very nature of things, and opinions are likely to differ. The accountant's duty is to record the transactions as entered into. His burden cannot be made an intolerable one. Needless to say, any such requirement is unsound and contrary to correct accounting principles.

VI. System Incomplete Without Provisions Criticised

If the provisions of the system of accounts which I have characterized as unsound or contrary to sound principles of correct accounting were removed from the system, it would not be a complete system of accounts. Essential parts would be missing and unless substitute provisions were written in to take their places it would be impossible

[fol. 407] to keep a set of accounts in accordance with the system.

(Sgd.) Jno. T. Madden.

Subscribed and sworn to before me this 6th day of December, 1935. (Sgd.) James W. Green, Notary Public. New York County Clerk's No. 171. New York County Reg. No. 7G223. My Commission Expires March 30, 1937. (Seal James W. Green, Notary Public, New York County.)

[fol. 408] [Title omitted]

AFFIDAVIT OF ROY B. KESTER

STATE OF NEW YORK,
County of New York, ss:

Roy B. Kester, being duly sworn on oath, deposes and says:

I reside at 440 Riverside Drive, New York, New York.

I am a Certified Public Accountant (Colorado). I have been a member of the Accounting Staff of the School of Business of Columbia University since 1915 and professor since 1922. I was in charge of research of the National Association of Cost Accountants from 1925 to 1929, both [fol. 409] inclusive. I am a member of the American Institute of Accountants and the American Association of University Instructors of Accounting of which body I was President, in 1929; of the National Association of Cost Accountants; and am a life member of the Colorado State Society of Certified Public Accountants. I was in charge of the investigation of wage levels in comparison with the standard of living of the Machine Tool Industry of the Newark District for the War Industries Board from 1918 to 1919. I gave expert testimony for the Government in the case of United States v. Samuel Insull, et al. I am author of "Accounting Theory and Practice," in three volumes, as follows: Volume 1, "Principles of Accounting"; Volume 2, "Advanced Accounting"; Volume 3, "Applications of Accounting Principles to Various Industries"; the above books being used extensively as texts in colleges and having sold to the extent of about a quarter of a million

copies. I have been a contributor to the American edition of Brittanica and Lippincott's encyclopedia and a contributor to numerous United States technical accounting and trade magazines, and I appeared on the program of the International Congress of Accountants held in New York in 1929.

I have examined the new system of accounts entitled "Uniform System of Accounts for Telephone Companies," prescribed by the Federal Communications Commission in [fol. 410] accordance with the provisions of the Communications Act of 1934, Issue of June 19, 1935, effective January 1, 1936, prescribed by an order of the Federal Communications Commission denominated Telephone Division Order No. 7-C.

I note the following somewhat unique and unusual requirements, comments on which are appended and constitute a part of this affidavit:

1. Definition of "Original Cost" or "Cost" (See Instruction 3-S.1, page 5 of the system of accounts).

2. The record of Telephone Plant Investment (See Balance Sheet Accounts, I. Investments, pages 26-27, and Instructions 20 and 21, pages 11-13).

* * * * * * *

5. Just and Reasonable Charges (See Instruction 2-B.1, page 2).

1. Definition of "Original Cost" or "Cost"

Comments

The above system of accounts provides two definitions of "Cost" as follows:

[fol. 411] (a) "Original Cost" or "Cost," as applied to telephone plant, etc., means the actual money cost—or equivalent—of property at the time when it was first dedicated to the public use, whether by the accounting company or by a predecessor public utility (Instruction 3-S. 1, page 5).

(b) "Cost," except as applied to telephone plant, etc., means the amount of money actually paid for property or services (Instruction 3-G. 1, page 4).

"Cost" as defined under (a) is quite unique from an accounting standpoint, in that it brings into the accounting records a cost basis which is not current cost and is therefore not the cost of the reporting company. It is a cost which may have been the result of price levels wholly different—i. e., higher or lower—from those prevailing at the time of purchase.

"Cost," in accordance with established accounting practice, is an individual matter. The records of an individual concern must show what its own costs are: never those of a competitor, nor what its own costs might have been had other conditions prevailed or other decisions been made than those which were made. In other words, the record of each concern must provide an accurate history of what actually took place in that concern.

[fol. 412] 2. The Record of Plant Investment

Comments

The above system of accounts sets up three property investment accounts, 100.1, 100.2 and 100.3, and requires that each shall state the "original cost" as so defined in the order. Thus Account 100.1 is to state the "original cost" of telephone plant in service, Account 100.2, the "original cost" of telephone plant under construction, and Account 100.3, the "original cost" of property held for imminent future telephone use.

In the case of purchased property, none of these accounts will show the actual cost to the accounting company (its actual investment), unless by coincidence the purchaser has paid the seller exactly what the property cost the original dedicator.

The difference between "the amount of money actually paid" for purchased property and the "original cost" of that property is to be stated in a separate account—100.4, "Telephone Plant Acquisition Adjustment." The amounts in this account "*shall* be disposed of, written off, or provision *shall* be made for the amortization thereof in such manner as the Commission may direct."

[fol. 413] No provision is made for the expense of depreciation with respect to the portion of the investment recorded in Account 100.4.

The amounts in Account 100.4 are not distributed among the plant accounts, i. e., "buildings," "pole lines," etc. (Accounts 201-277, pages 47-61.)

In so far as the company's property consists of plant purchased from another utility at prices different from the cost to the original dedicator, neither the Accounts 100.1, "Telephone Plant in Service," 100.2, "Telephone Plant Under Construction" and 100.3, "Property Held for Future Telephone Use," nor the so-called plant accounts ("buildings," "pole lines," etc.) will show the actual cost to the accounting company of the property covered by those accounts. Instead of showing the investment of the owner in such property, they will show the investment of some prior owner.

The difference between the owner's investment and the investment of the prior owner will be shown temporarily in an "adjustment" account, but this must be extinguished, either immediately or later, at the pleasure of the Commission. The company is not allowed to recover, through depreciation charges, its own investment in property which is being used up, but must base its depreciation charges on the investment of some prior owner.

[fol. 414] These requirements are in my opinion contrary to the fundamental principles of correct accounting for the following reasons:

(a) Sound accounting requires that the accounts of a company shall correctly record the transactions of that company and truly reflect its condition.

(b) To this end it is universally recognized that sound practice requires that a company's plant accounts shall reflect its own actual costs.

(c) It is unsound and unheard of to keep a company's accounts neither on the basis of cost to it nor of value, but on the basis of the costs of some one else for which the accounting company has no responsibility. Accounts kept on such a basis would be misleading to the public, to investors, to the company's management, to legislatures, to future regulatory bodies, to taxing authorities and to the courts. The system of accounts requires the accounts to be kept on this unsound basis. It is true that so long as the "difference" remains in the "adjustment" account, it is

technically listed as an asset of the company, but since its extinction is mandatory and may be immediate if the Commission so wills, it would not be regarded as an asset in anything but name. The accounts list it as an asset, but label it as an asset to be charged off, and therefore im- [fol. 415] pliedly worthless. In actuality, it is a deferred charge against surplus, since the Commission can make it such a charge at any time, and the company could not safely regard it except as a deduction from surplus. In practical effect, the situation is no different while the amounts in Account 100.4 are listed among the assets than it is after they are charged off.

After they have been charged off, the company's accounts will nowhere reflect the actual cost of its property, even nominally.

(d) The system of accounts requires that even where a company has purchased property at its actual, undisputed value, and where there has been no change in value, if that price happens to be higher than the price the original dedicator paid for it, the company must submit to having the difference charged off. To thus require a company's accounts to record a loss which has not occurred is contrary to all recognized principles of accounting.

Depreciation as Related to Account 100.4

It is a fact that a company's investment is gradually impaired by the using up of the property in which the investment has been made. Sound accounting requires that this fact be recognized in the accounts. The system of [fol. 416] accounts purports to recognize this principle by requiring depreciation charges to be made with respect to property which is thus used up, but these charges are not permitted to be made against the balance in Account 100.4. Depreciation charges are permitted to be made only against the "original cost" of the property. The effect is that the accounts will not record the impairment of the company's own investment, but will record, so far as purchased property is concerned, a depreciation expense which is related only to the investment of some one else. This is obviously contrary to sound accounting principles.

Distinctions in Classification of Plant

As stated above, the system of accounts requires that the "original cost" of a company's telephone plant shall be recorded in one of three accounts: 100.1, "Telephone Plant in Service," which shall include plant "used" in telephone service at the date of the balance sheet; 100.2, "Telephone Plant Under Construction"; and 100.3, "Property Held for Future Telephone Use," which shall include "property owned and held for imminent use in telephone service under a definite plan for such use." In addition to the above record, provision is made for another account, viz., Account 103, "Miscellaneous Physical Property," which shall [fol. 417] include all other physical property.

In connection with Account 100.3, the word "imminent" is too vague to define a precise accounting classification. There could obviously be the widest difference of opinion as to whether the use of property was imminent. To one accountant it might mean within a month and to another it might mean anything within a year or two years. This definition must be made more specific if accountants are to know what property to charge to Account 100.3 and what to Account 103. The definition as it stands is subject to such variation in construction as to be destructive of uniformity in accounting and to leave accountants at a loss as to which account to use.

Accountants will also experience great difficulty in determining what property is "used" in telephone service—Account 100.1—as distinguished from that "held for imminent use"—Account 100.3. I am informed that in the telephone business a large part of the total property consists of large units, such as a cable, which in turn consists of many pairs of fine wires, only part of which may be in use at a given time. I am informed that in such a case it has been contended by accountants for some regulatory bodies that since only a part of the wires in the cable are in use only a part of the cable is "used" in telephone service, while the companies contend that when some wires in a [fols. 418-420] cable are in use the cable itself is "used." I am also informed that small items of telephone plant, such as a pair of wires in a cable or a circuit in a switchboard go in and out of service continually as telephones are installed or removed, as plant goes out of order temporarily

and as traffic ebbs and flows. In such a state of facts the words "used in telephone service" and "held for imminent use" are too vague to distinguish adequately the one from the other, accountants would not know definitely to which account plant should be charged and there would be bound to be a variation of opinion which would be destructive of uniformity. Under the Interstate Commerce Commission's Uniform System of Accounts for Telephone Companies, First Revised Issue, all telephone plant was grouped in a single account "Telephone Plant" and these inherently difficult lines of distinction were avoided.

* * * * * * * *

[fol. 421] 5. Just and Reasonable Charges

Comments

The system of accounts under this order requires that [fol. 422] all charges to plant investment, income, operating revenue and operating expense accounts shall be "*just and reasonable*" and that any payments by plaintiffs in excess of such just and reasonable charges shall be charged against income. What are just and reasonable payments must necessarily be, to a considerable extent, a matter of judgment, as to which opinions are likely to differ widely. Accountants, instead of merely recording the facts of the company's transactions, would have to investigate each transaction to see if the payment had been reasonable, and even then in many instances there could not be uniformity of judgment. Any such procedure is unheard of in accounting, is contrary to sound principles and would produce chaotic results. The function of accounts is to reflect the facts, whatever they may be, and not to record the accountant's judgment as to what the facts should have been.

6. System Incomplete Without Provisions Criticized

If the provisions of the system of accounts which I have characterized as unsound or contrary to sound principles of correct accounting were removed from the system, it would not be a complete system of accounts. Essential [fol. 423] parts would be missing and unless substitute provisions were written in to take their places it would be

impossible to keep a set of accounts in accordance with the system.

(Sgd.) Roy B. Kester.

Subscribed and sworn to before me this 6th day of December, 1935. (Sgd.) Charles M. Deal, Notary Public, Kings Co., No. 363. Reg. No. 7148, Cert. Filed in N. Y. Co. No. 393, Reg. No. 7-D-225. Commission expires March 30, 1937. (Seal.)

[fol. 424] [Title omitted]

AFFIDAVIT OF B. F. YOUNG

STATE OF NEW YORK,
County of New York, ss:

B. F. Young, being duly sworn on oath, deposes and says:

I reside at 62 Belvidere Place, Yonkers, New York.

I am General Auditor of the New York Telephone Company, one of the plaintiffs herein. I did graduate work in statistics at Columbia University and received the degree [fol. 425] of Master of Arts from that institution. I lectured on statistics at New York University for a period of approximately five years. Since 1919 I have been in the Accounting Department of the New York Telephone Company and since 1923 have held successively the positions of Assistant Chief Accountant, Chief Accountant, Assistant General Auditor and General Auditor, the latter position since 1933. During my entire service with the New York Telephone Company the making of estimates of the cost of various accounting methods and procedures for use in the economical and efficient management of the company's accounting has been an important and continuing part of my work. As General Auditor I have entire responsibility for the administration of the company's accounting work and for the application to the company's accounting of systems of accounts prescribed by regulatory bodies. I have supervision of the accounts and the accounting records of the company and I am thoroughly familiar with the steps and processes by which the accounting work of the company is carried on.

I have carefully examined the "Uniform System of Accounts for Telephone Companies, Issue of June 19, 1935, Effective January 1, 1936," prescribed by the Federal Communications Commission. For some time prior to the is- [fol. 426] suance of said system I had been giving careful consideration to the effect upon the company's accounting costs of many of the proposed provisions which were subsequently incorporated therein, and since the issuance thereof I have had careful and detailed studies made under my supervision and direction of the cost to the company of complying with the various provisions of the new system.

Among such studies was a detailed study of the cost to the New York Telephone Company of restating its plant accounts on the basis of "original cost" (estimated if not known) as required by said system. In the case of a large part of the purchased plant of the company it will be impossible to ascertain the "original cost" and it will therefore be necessary to estimate it. In many cases it will be impossible to make such estimates except by mere guesswork but a great deal of work will be required in order to ascertain what, if any, data exists upon which estimates may be based. This study was designed to find out how much it would cost to ascertain "original cost" where the same could be ascertained, and to obtain the necessary data upon which to base estimates where such data exists. Such study included consideration of the pertinent facts and the making of careful estimates based thereon of the cost of the various elements entering into the cost of restatement, [fol. 427] and it showed that the total cost of restatement would be $432,100.00. While this study cannot in the nature of things show what the exact cost to the company would be, I am of the opinion that it is a reliable estimate and that the total cost to the company of restating its plant accounts as aforesaid would be in the neighborhood of the amount stated.

Among the studies referred to above was a study of the cost to the New York Telephone Company of complying with the requirement of said new system of accounts that plant which is "used in telephone service" shall be included in Account 100.1 and that all other telephone plant- shall be included in Account 100.3, as property held for imminent [fol. 428] use in telephone service, or in other accounts. Whether plant is "used in telephone service" is, because

of the nature of the telephone business, a matter which is subject to a wide variety of interpretation. The system of accounts gives no indication of how finely plant shall be divided in determining what parts of it are in use, and it has therefore been necessary to make assumptions as to this. For the purposes of the study I assumed that when a telephone is taken out the pair of wires (whether in cable or otherwise) connecting that telephone with the central office is no longer used in telephone service and must therefore be transferred from Account 100.1 to Account 100.3. I have assumed that a vacant duct in a conduit, and a complete section of switchboard or a complete cable terminal, to which no working line was connected, would be carried in Account 100.3. On the other hand, I have assumed that a section of switchboard, to which any working line was connected, would be regarded as "used in telephone service" and carried in Account 100.1, regardless of the fact that many of the lines attached thereto were not in use, and I have made the same assumption with regard to a cable terminal with which any working line was connected. I have also assumed that where a telephone building was in use the entire building would be regarded "used in tele-
[fol. 429] phone service" and carried in Account 100.1 even though there might be a considerable amount of vacant space therein. A study based on the above assumptions and assumptions on the same general basis as to other classes of plant shows that the cost to the New York Telephone Company of transferring property in and out of Account 100.1 as it became used or unused in telephone service, would be $1,177,700.00 per year, and that the cost for the first year, including the cost of establishing the segregation initially, would be $4,187,395.00. While in the nature of things these studies cannot show exactly what the costs would be, they have been carefully made and I consider them to be reliable estimates.

(Sgd.) B. F. Young.

Subscribed and sworn to before me this 6th day of December, 1935. (Sgd.) Charles M. Deal, Notary Public. Notary Public, Kings Co., No. 363, Reg. No. 7148. Cert. Filed in N. Y. Co. No. 393, Reg. No. 7-D-225. Commission Expires March 30, 1937. (Seal.)

[fol. 430] [Title omitted]

AFFIDAVIT OF CHARLES A. HEISS

STATE OF NEW YORK,
County of New York, ss:

Charles A. Heiss, being duly sworn on oath, deposes and says:

I reside at East Orange, New Jersey, and am Comptroller of the American Telephone and Telegraph Company, one of the plaintiffs herein, having my office at 195 Broadway, New York City. I graduated from the College of Political Sciences, George Washington University, with the degree of Bachelor of Arts, pursued graduate study at [fol. 431] the University of Michigan, and was later awarded an honorary degree of Master of Arts from the University of Michigan. I spent approximately six years in the service of the Interstate Commerce Commission in its Accounting and Statistical Departments, three years of which period were spent as assistant to Dr. Henry C. Adams, Dean of the Department of Economics, University of Michigan, while he was in charge of accounts and statistics for the Commission, and engaged extensively in the development of Uniform Systems of Accounts for classes of companies, the accounts of which were subject to the jurisdiction of the Interstate Commerce Commission. I held the position of Examiner of Accounts in its Bureau of Accounts at the close of my service. I also participated actively on the program of the International Congress of Accounting held in New York City in 1929. Since 1913 I have ben in the service of the American Telephone and Telegraph Company, hereinafter called the "American Company," and have now been Comptroller of that company for fifteen years.

Plaintiff, The Home Telephone and Telegraph Company of Spokane, transferred all of its property to The Pacific Telephone and Telegraph Company and ceased to be a carrier on December 1, 1935, and where the term "plain-[fol. 432] tiffs" is hereinafter used it is not intended to include The Home Telephone and Telegraph Company of Spokane.

As Comptroller I have supervision over and access to all the books of account and accounting records of the

American Company. With the exception of The Cincinnati and Suburban Bell Telephone Company and The Southern New England Telephone Company, in which the American Company owns approximately one-third of the stock, all of the other plaintiffs are controlled either directly or indirectly by the American Company through stock ownership, and each of the plaintiffs is a member of the group of affiliated companies known as the "Bell System." As a part of my duty as Comptroller of the American Company, I have for many years kept myself informed as to the accounting practices of the other companies in the Bell System and with their condition as reflected by their accounts. All of the plaintiffs have kept their accounts in accordance with the accounting system from time to time prescribed by the Interstate Commerce Commission, as alleged in the Bill of Complaint, and I have been at all times familiar with said system. The auditors in my department have for many years audited the accounts of all of the plaintiffs, with the exception of four of the smaller companies which [fol. 433] are indirectly controlled, namely: The Tri-State Telephone and Telegraph Company, Dakota Central Telephone Company, Christian-Todd Telephone Company and The United Telephone Company, and I and many members of my staff, working under my direction, have had frequent contacts with the accounting staffs of all of the plaintiffs (with the four exceptions specified), who have relied on my department for advice and assistance in their accounting. I have for many years received detailed monthly reports from all of the plaintiffs, with the four exceptions specified, and I have familiarized myself with the accounting practices and the condition of the said four companies by means of other reports and through contact with the accounting officers who have general knowledge of their accounts and supervision of audits thereof.

Portions of the property of all of the plaintiffs have been acquired by them from other public utility companies and in many cases the vendor companies had acquired the property from still other public utility companies. It is impossible to make more than a very rough estimate of the amount of the property so acquired which is still in existence. In addition to many acquisitions of operating plants as a whole the plaintiffs have purchased from other tele- [fol. 434] phone companies, from electric light companies,

telegraph companies, and railroads, many small quantities of plant, such as a section of pole line or a single pole, or a fractional interest therein. There have been a very large number of individual transactions of this kind by the plaintiffs and their predecessor companies—certainly more than a hundred thousand in the last twenty years and probably considerably more. When purchased, this property has become commingled with other property of the purchasing company, and when retired it has not been distinguished from other property retired. Since 1915 the plaintiffs, in the aggregate, have acquired from other public utilties property which was placed on their books at approximately $750,000,000. Of this amount, approximately $500,000,000 has been acquired from companies in which plaintiffs owned all or substantially all of the stock, and has been accounted for by merging the book accounts of the companies, the property thus being placed on the books of the acquiring company at cost to the predecessor company, but not at "original cost" as defined by the Commission, because in many cases part of it had been purchased by the predecessor and placed on its books at the purchase price. The remaining $250,000,000 of acquired property (acquired partly from affiliated and partly from independent com- [fol. 435] panies) has been recorded on the books of plaintiffs at its actual cost to them, except that minor amounts, acquired since January 1, 1933, when the Interstate Commerce Commission's revised system of accounts became effective, have been accounted for at current cost new, with an offsetting entry for depreciation. Much of this $250,000,000 of purchased property is no longer in existence and has been written off the books of plaintiffs. Taking into consideration the dates upon which the purchases were made and the general, overall life of telephone plant, as well as knowledge of some of the larger elements which remain in service, I estimate that of said $250,000,000.00 of purchase property, well over $100,000,000 of property is still in existence, that portions of this are now in the plants of all of the plaintiffs, in amounts ranging from $250,000 to $12,000,000 except in the case of the Christian-Todd Telephone Company, The Diamond State Telephone Company, The Cincinnati and Suburban Bell Telephone Company and the Bell Telephone Company of Nevada, where the amounts are smaller.

All acquisitions of property since January 1, 1913, have been accounted for as required or permitted by the Interstate Commerce Commission or the Federal Communications Commission, and practically all the acquired property [fol. 436] of plaintiffs which is now in existence has been acquired since that date.

I have examined and am familiar with the system of accounts prescribed by the Federal Communications Commission entitled "Uniform System of Accounts for Telephone Companies, Issue of June 19, 1935, Effective January 1, 1936," the enforcement of which this suit seeks to enjoin.

Said system, in Instruction 3-S. 1, defines "original cost," as applied to telephone plant, as the cost of the property at the time when it was first dedicated to the public use, whether by the accounting company or by a predecessor public utility. The system provides that each of three property investment accounts, Account 100.1, "Telephone Plant in Service," Account 100.2, "Telephone Plant Under Construction," and Account 100.3, "Property Held for Future Telephone Use," shall state the "original cost," as so defined, of the property embraced therein. Because of their requirement none of these accounts can show, in the case of purchased property, the actual cost of the property to the accounting company (the accounting company's actual investment) unless by coincidence.

Said system requires in effect that the difference between the cost to the purchaser and the cost to the original dedi- [fol. 437] cator shall be stated on the purchasing company's books in a separate account, 100.4, "Telephone Plant Acquisition Adjustment," and that the amounts in this account "shall be disposed of, written off, or provision made for the amortization thereof in such manner as the Commission may direct." I say that this is the requirement "in effect" because to the difference (between cost to the purchaser and "original cost") when entered in Account 100.4 there is added the amount of the depreciation reserve requirement, but as this amount is offset by a corresponding entry in the reserve account on the liability side, it has no effect of the net assets and may properly be ignored in stating the effect of the accounting requirement. (See Account 100.4 at page 27 of Exhibit B attached

to the Bill of Complaint herein and Instruction 21 at pages 12-13 of said exhibit.)

Said system includes a series of accounts (201 to 277 inclusive) which are entitled "Telephone Plant Accounts" and which show separately the "original cost," as defined, of the various classes of the company's property, such as buildings, central office equipment and aerial cable. These accounts are in effect subaccounts of Account 100.01, and the entries in Account 100.4 are not distributed among these subaccounts. The telephone plant accounts, therefore, can- [fol. 438] not show the company's actual investment in the various classes of its plant, if it has any purchased property, except possibly by coincidence.

Said system makes no provision for charging anything for the expense of depreciation with respect to the portion of the company's investment recorded in Account 100.4. By Instruction 80 (page 22 of said Exhibit B) the company is confined to charging depreciation expense by applying the applicable percentage rates to the "original cost," as defined, of the various classes of depreciable property.

The effect of these requirements, in so far as the company's property consists of plant purchased from another utility at prices different from the cost to the original dedicator, is that neither Accounts 100.1, "Telephone Plant in Service," 100.2, "Telephone Plant Under Construction," 100.3, "Property Held for Future Telephone Use," nor the several telephone plant accounts (buildings, pole lines, etc.), will show the cost to the company of its property covered by those accounts. Instead of showing the investment of the owner in such property they will show the investment of some prior owner. The difference between the owner's investment and the investment of the prior owner will be [fol. 439] shown temporarily in an "adjustment" account, but this must be extinguished, either immediately or later, at the pleasure of the Commission. While this "difference" is technically listed as an asset of the company so long as it remains in the "adjustment" account, it will not be regarded as an asset in anything but name, since its extinction is mandatory and may be immediate if the Commission so wills. The accounts list it as an asset, but label it as an asset to be charged off and therefore impliedly worthless. In actuality it is a deferred charge against surplus, since the Commission can make it such a charge at any time.

Therefore the company could not safely regard it as anything except a deduction from surplus, in effect freezing an equivalent amount thereof. In practical effect the financial position will be no different while the amounts in the "adjustment" account (Account 100.4) are listed among the assets than it will be after they are charged off. After the amounts in Account 100.4 have been charged off, the company's accounts will nowhere reflect the actual cost of its property, even nominally. The effect will be that, even where a company has heretofore purchased property at its actual, undisputed value and where there has been no change in value, if that price happens to be higher than the price the original owner paid for it, the company must re- [fol. 440] cast its accounts and submit to having the difference charged off, and it must likewise submit to the writing off of a loss which it has not incurred whenever, in the future, it may purchase property at a price which, although representing its actual value, is higher than its cost to the predecessor public utility which first dedicated it to the public use.

In so far as the company's property consists of plant purchased from another utility at prices different from the cost to the original dedicator, said system does not allow the company to recover, through depreciation charges, its own investment in property which is being used up in service, but requires it to base its depreciation charges on the investment of some prior owner.

Sound accounting requires that the accounts of a company shall correctly record the facts of its transactions, whatever those facts may be, and shall truly reflect its condition. It is universally recognized that sound accounting practice requires that a company's accounts shall reflect its own actual costs. There are occasional departures from this rule, as in the case of inventories, which may be periodically revalued, or in the case of assets which have become worthless and are therefore written off. But it is unsound, [fol. 441] unprecedented and contrary to the fundamental principles of correct accounting to keep a company's accounts neither on the basis of cost to it nor of value, but on the basis of the cost to some one else for which the accounting company has no responsibility. It is equally unsound and contrary to all recognized principles of accounting to require a company's accounts to record a loss which

has not occurred and to require it to record, instead of depreciation upon the company's own investment, a depreciation expense which is related only to the investment of some one else. Accounts kept on such a basis would be misleading.

Said system of accounts requires that as of January 1, 1936, plaintiffs shall restate their then existing property investment accounts by eliminating from the recorded cost all property theretofore acquired by them from another public utility and substituting for such recorded cost the amount (estimated if not known) which said property cost the former owner who first dedicated it to public use. In the case of a majority of the purchased property now owned by the plaintiffs this accounting is impractical if not impossible of application and could not be carried out except by mere guesswork. Under the accounting heretofore and now in effect, the property of the plaintiffs has been charged to [fol. 442] various plant investment accounts, such as pole lines, aerial cable and station apparatus (telephones). When units of property have been retired from service they have been written out of the plant investment accounts, usually at their average cost, so that it has been unnecessary to identify individual items of property, such as an individual pole or an individual telephone, for purposes of accounting. The purchased property has become commingled with property built by the plaintiffs themselves and much property of both kinds has been retired so that it would now be virtually impossible to establish the identity of items of purchased property in the great majority of cases. Unless such identity could be established it would be necessary to estimate what purchased items remained in the plant and then to estimate their date of installation in order to obtain a price level existing at that date for use in estimating the "original cost." The books and records of the company first devoting the purchased property to public use are in many cases not available and where they are available such books and records in many cases do not show either the "original cost" of the property or the dates of installation, and the undertaking would be a practically fruitless one. The searching of the records of plaintiffs and their predecessor [fols. 443 & 444] companies, including the records of the many thousands of small purchases over a long period of years, in an effort to establish such of the facts as could be

established, would require the expenditure by plaintiffs of several millions of dollars.

Said accounting would be impractical of application to purchases made in the future unless the amount recorded in Account 100.4 should be immediately written off, because it would require the separation of the investment in a single item of purchased property, such as a pole, into two accounts, and when it become necessary to write an item out of the accounts, upon retirement, there would be no practical way of finding out whether the item retired was one which had been charged in part to a plant account and in part to Account 100.4, or was a non-purchased item which had been charged to the plant account in its entirety. This difficulty could be overcome only by tagging and keeping records of each small item of property, which would add greatly to the accounting expense of plaintiffs.

[fol. 445] Said system of accounts requires that the "original cost" of all of the company's physical property, except telephone plant under construction, shall be recorded in one of three acounts, 100.1, "Telephone Plant in Service," which shall include plant "used" in telephone service at the date of the balance sheet, 100.3, "Property Held for Future Telephone Use," which shall include "property owned and held for imminent use in telephone service under a definite plan for such use" and 103, "Miscellaneous Physical Property," which shall include all other physical property. To comply with these require-

[fol. 446] ments property which is not used must be recorded in Account 100.3 if its use is imminent under a definite plan, and in Account 103 if its use is not imminent or if there is no definite plan. The word "imminent" is too vague to define an accounting classification. There could obviously be the widest difference of opinion as to whether the use of property was imminent. To one accountant it might mean within a month and to another it might mean within a year or two years. The addition of the words "definite plan" does not mitigate this uncertainty because the use must be imminent if property is to be recorded in Account 100.3, and if its use is not imminent it must be recorded in Account 103 even though the plan be definite. The dividing line between these classifications as prescribed in said system is so lacking in precision and subject to such a wide variation in construction as to be destructive

of uniformity in accounting and to leave accountants at a loss as to which account to use.

In order to determine whether property should be charged to Account 100.1, "Telephone Plant in Service" or Account 100.3, "Property Held for Future Telephone Use," it will be necessary for the accountants to decide what property is "used" in telephone service as dis- [fol. 447] tinguished from that "held for imminent use." In the telephone business a large part of any company's total property consists of large units such as a cable, which in turn consists of many pairs of fine wires, only a part of which may be in use at any given time. It has been contended that since only a part of the wires in a cable are in use only a part of the cable is "used" in telephone service, while the telephone companies contend that when some wires in a cable are in use the cable itself is "used." The same difference of opinion exists in regard to an underground conduit which is divided by partitions into a number of passageways or ducts, only a part of which may contain cables at a given time, and in regard to vacant floor space in telephone buildings, partially filled switchboards and many other items of telephone plant which in the aggregate constitute a very large part of the property of the plaintiffs herein. It is likewise a fact that small items of telephone plant, such as a pair of wires in a cable or a circuit in a switchboard go in and out of service continually as telephones are installed or removed, as plant goes out of order temporarily and as traffic ebbs and flows. In such a state of facts in view of the controversy on this subject and the cases now pending before courts and commissions, [fol. 448] the words "used in telephone service" and "held for imminent use" are too vague to adequately distinguish the one account from the other, accountants would not know definitely to which account plant should be charged and there would be a variation of opinion which would be destructive of uniformity in accounting.

[fol. 449] Instruction 2. B. 1 of the system of accounts (page 2) requires that all charges to the accounts prescribed for telephone plant, income, operating revenues and operating expenses, shall be just and reasonable and [fol. 450] that any payments by the company in excess of such just and reasonable charges shall be charged against income. What are just and reasonable payments must

necessarily be, to a large extent, a matter of judgment, as to which opinions are likely to differ widely. Under this requirement the company's accountants, instead of recording the facts of the company's transactions, would have to investigate each transaction to see if the payment had been reasonable, and the judgment of different accountants in similar cases would be bound to vary widely. Any such procedure would be destructive of uniformity in accounting, would produce chaotic results and would be contrary to the basic principles of accounting in that the function of accounts is to reflect the facts, for example, the facts as to what the company's operating expenses actually were rather than some one's judgment as to what the operating expenses should have been.

It is necessary that the plaintiffs keep accounts which accurately record the facts of their transactions and truly reflect their actual condition for the information of their officers and directors, so that they may manage the business intelligently, may make accurate reports to taxing authorities and regulatory bodies, and may make true representations to prospective investors. Such accounts are also [fol. 451] necessary for the information of the stockholders of the plaintiffs. The Uniform System of Accounts for Telephone Companies, First Revised Issue, prescribed by the Interstate Commerce Commission, pursuant to which the accounts of the plaintiffs are now kept, is, in my judgment, a system of accounts which is adequate for the foregoing purposes and which is on the whole a sound accounting system. The Uniform System of Accounts for Telephone Companies, Issue of June 19, 1935, effective January 1, 1936, prescribed by the Federal Communications Commission, is, in my judgment, inadequate for the foregoing purposes, since it would be misleading and would conceal relevant facts in the particulars hereinabove specified. The plaintiffs have for many years filed with governmental agencies, such as regulatory bodies and taxing authorities, and have directly or indirectly issued to investors and to the public financial statements taken from their books of account as heretofore kept, and said books of account have formed the basis of their corporate financing and other important corporate activities. The recasting of the completed accounts, which would be required in order to conform to said system prescribed by the Federal Communica-

tions Commission, would result in the publication of finan- [fol. 452] cial statements substantially different from those heretofore issued which would, in effect, contradict those upon which the financial structures of the plaintiffs have been based. In my judgment the publication of such contradictory statements would impair the confidence of investors in the accounts of the plaintiffs and would consequently impair their credit.

Said system of accounts prescribed by the Federal Communications Commission is designed as a complete accounting system. If the provisions hereinabove criticized and characterized as unsound and contrary to correct accounting principles should be stricken from the system, vital and necessary parts of it would be missing, and unless substituted provisions were written in to take their places, it would be impossible to keep accounts in accordance with it. [fol. 453] The Uniform System of Accounts for Telephone Companies, First Revised Issue, prescribed by the Interstate Commerce Commission, under which the accounts of all of the plaintiffs are now kept, does not contain any of the requirements complained of in the Bill of Complaint [fols. 454-460] herein and hereinabove criticized. A copy of said First Revised Issue is hereto attached and marked Appendix B.

(Sgd.) Charles A. Heiss.

Subscribed and sworn to before me this 6th day of December, 1935. (Sgd.) Charles M. Deal, Notary Public. Notary Public, Kings Co., No. 363, Reg. No. 7148. Cert. Filed in N. Y. Co. No. 393, Reg. No. 7-D-225. Commission Expires March 30, 1937. (Seal.)

Uniform System of Accounts

for

Telephone Companies

PRESCRIBED BY THE

INTERSTATE COMMERCE COMMISSION

IN ACCORDANCE WITH SECTION 20 OF THE
INTERSTATE COMMERCE ACT

For Class A Companies
Effective on January 1, 1933

For Class B Companies
Effective on January 1, 1934

First Revised Issue

UNITED STATES
GOVERNMENT PRINTING OFFICE
WASHINGTON : 1932

For sale by the Superintendent of Documents, Washington, D. C. - - - Price 10 cents

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ORDER

At a Session of the INTERSTATE COMMERCE COMMISSION, Division 4, held in its office in Washington, D. C., on the 12th day of November, A. D. 1932

The subject of a Uniform System of Accounts to be prescribed for and kept by telephone companies being under consideration, the following order was entered:

It is ordered, That the Uniform System of Accounts for Telephone Companies with the text pertaining thereto, embodied in printed form to be hereafter known as First Revised Issue, a copy of which is now before this Commission, be, and the same is hereby, approved; that a copy thereof duly authenticated by the Secretary of the Commission be filed in its archives, and a second copy thereof, in like manner authenticated, in the office of the Bureau of Accounts; and that each of said copies so authenticated and filed shall be deemed an original record thereof.

It is further ordered, That the said Uniform System of Accounts for Telephone Companies with the text pertaining thereto, be, and the same is hereby, prescribed for the use of telephone companies having annual operating revenues exceeding $50,000, subject to the provisions of the interstate commerce act, in the keeping and recording of their accounts; that each and every such carrier and each and every receiver or operating trustee of any such carrier be required to keep all accounts in conformity therewith; and that a copy of the said First Revised Issue be sent to each and every such carrier and to each and every receiver or operating trustee of any such carrier.

It is further ordered, That in order that the basis of comparison with previous years be not destroyed, any such carrier or any receiver or operating trustee of any such carrier may, during the twelve months from the time that the said First Revised Issue becomes effective,

keep and maintain, in addition to the accounts hereby prescribed, such portion or portions of its present accounts as may be deemed desirable by any such carrier, or by any receiver or operating trustee thereof, for the purpose of such comparison; or, during the same period, may maintain such groupings of the primary accounts hereby prescribed as may be desired for that purpose.

It is further ordered, That any such carrier or any receiver or operating trustee of any such carrier, in addition to the accounts hereby prescribed, may unless otherwise ordered, keep any temporary or experimental accounts the purpose of which is to develop the efficiency of operation: *Provided, however*, That such temporary or experimental accounts shall not impair the integrity of any primary account hereby prescribed.

It is further ordered, That any such carrier or receiver or operating trustee of any such carrier, may subdivide the accounts hereby prescribed to the extent necessary to secure the information required in the prescribed reports to commissions having jurisdiction.

It is further ordered, That the dates on which the said First Revised Issue of the Uniform System of Accounts shall become effective, be, and are hereby, fixed for Class A Telephone Companies on January 1, 1933, and for Class B Telephone Companies on January 1, 1934, provided that Class B Telephone Companies are permitted to adopt this system of accounts on January 1, 1933.

By the commission, division 4.

[SEAL.] GEORGE B. MCGINTY,
Secretary.

INTRODUCTORY LETTER

INTERSTATE COMMERCE COMMISSION,
THE BUREAU OF ACCOUNTS,
Washington, D. C., November 12, 1932.

TO TELEPHONE COMPANIES:

This Uniform System of Accounts for Telephone Companies will supersede the Uniform System of Accounts for Telephone Companies, First Issue; effective January 1, 1913.

Under the interstate commerce act, the observance of the rules and regulations stated in this system of accounts becomes obligatory upon persons having direct charge of the accounts of the companies concerned, and such persons will be held responsible for their proper application.

Paragraph 6 of the twentieth section of the interstate commerce act provides that—

> In case of failure or refusal on the part of any such carrier, receiver, or trustee to keep such accounts, records, and memoranda on the books and in the manner prescribed by the Commission, or to submit such accounts, records, and memoranda as are kept to the inspection of the Commission or any of its authorized agents or examiners, such carrier, receiver, or trustee shall forfeit to the United States the sum of five hundred dollars for each such offense and for each and every day of the continuance of such offense, such forfeitures to be recoverable in the same manner as other forfeitures provided for in this Act.

In formulating this system of accounts this bureau enlisted the cooperation of State commissions and of telephone companies. All suggestions and criticisms of these parties have been given most careful consideration. Many of the suggestions have been incorporated in these accounting rules.

Condensed classifications have been provided for operating revenues and operating expenses of companies having annual operating revenues exceeding $50,000 but not more than $100,000.

The provisions of the order under 14700, Depreciation Charges for Telephone Companies, have been appropriately included in this system of accounts.

The revised rules for telephone companies having average annual revenues not exceeding $50,000 will subsequently be given consideration.

This bureau will be glad to give consideration promptly to all questions arising with regard to the correct interpretation of this system of accounts which are presented to it by the officers in charge of accounts of telephone companies.

In case the carrier finds it is not in position to install upon the date specified all records necessary to comply with this system of accounts and furnishes a statement giving full facts as to its situation and the causes therefor, with a request to defer the complete installation of the accounts to a period within or at the close of the calendar year 1933, such a request to defer complete adoption of this Uniform System of Accounts will be given consideration by this Commission. The accounts contained herein as compared with those now effective are not materially so different as to prevent the returns to this Commission in the annual reports for the year 1933 being stated in accordance with these rules. Such returns will therefore be required to be in accordance with this system of accounts.

ALEXANDER WYLIE, *Director.*

INSTRUCTIONS

GENERAL

1. **Classification of companies.**—(A) As of the effective date of this system of accounts, for the purpose of accounting, telephone companies are divided into three classes as follows:

Class A.—Companies having average annual operating revenues exceeding $100,000.

Class B.—Companies having average annual operating revenues exceeding $50,000, but not more than $100,000.

Class C.—Companies having average annual operating revenues not exceeding $50,000.

(B) Class A companies shall keep all the accounts of this system of accounts, which are applicable to their affairs.

(C) Class B companies shall keep all the accounts of this system of accounts, which are applicable to their affairs, except that their accounts for operating revenues and expenses may be kept under the accounts of the condensed classification shown on pages 61, 64, and 65.

(D) This system of accounts is not prescribed for Class C companies.

NOTE.—In order that frequent changes may be avoided, companies operating established telephone plants may adopt the scheme of accounts indicated by the average of their annual revenues for three years immediately preceding the effective date of this order. If at the close of any calendar year the average of the annual revenues for the three latest years is greater than the amount applicable to the class in which the company has been accounting, the higher scheme of accounts shall be adopted. New companies shall estimate the amount of their annual revenues and adopt the scheme of accounts appropriate for the amount of such estimated revenues.

2. **Records.**—(A) The company's records shall be kept with sufficient particularity to show fully the facts pertaining to all entries in these accounts. Where the full information is not recorded in the general books the entries therein shall be supported by other records in which the full details shall be shown and the general book entries shall contain sufficient reference to the detail records to permit ready identification. The detail records shall be filed in such manner as to be readily accessible for examination by representatives of this Commission.

(B) Attention is directed to the following extract from the twentieth section of the interstate commerce act:

"Any person who shall willfully make any false entry in the accounts of any book of accounts or in any record or memoranda kept by a carrier, or who shall willfully destroy, mutilate, alter, or by any other means or device falsify the record of any such account, record, or memoranda, or who shall willfully neglect or fail

to make full, true, and correct entries in such accounts, records, or memoranda of all facts and transactions appertaining to the carrier's business, or shall keep any other accounts, records, or memoranda than those prescribed or approved by the Commission, shall be deemed guilty of a misdemeanor, and shall be subject, upon conviction in any court of the United States of competent jurisdiction, to a fine of not less than one thousand dollars nor more than five thousand dollars or imprisonment for a term not less than one year nor more than three years, or both such fine and imprisonment: *Provided*, That the Commission may in its discretion issue orders specifying such operating, accounting, or financial papers, records, books, blanks, tickets, stubs, or documents of carriers which may, after a reasonable time, be destroyed, and prescribing the length of time such books, papers, or documents shall be preserved."

The Commission's order specifying records which may be destroyed is contained in its "Regulations to Govern the Destruction of Records."

(C) Accounts which are clearly summaries of other accounts or subaccounts provided for herein (for example, account 100, "Telephone plant," which summarizes the balances in the telephone plant accounts or account 154, "Funded debt," which summarizes the balances in the several funded-debt subaccounts) are not required to be kept in the company's books. All accounts kept shall conform in numbers and titles to those prescribed herein, except that:

(1) Companies may subdivide any of the accounts, provided such subdivisions do not impair the integrity of the accounts prescribed. The titles of all such subdivisions or subaccounts shall refer by number or title to the accounts of which they are subdivisions. When subaccounts are thus kept, it is not required that the main accounts of which they are subdivisions shall also be kept in the company's books.

(2) Clearing accounts, in addition to those prescribed herein, may be kept when necessary in making the proper distribution of items to the appropriate primary accounts.

(3) Temporary or experimental accounts may be kept in addition to the accounts prescribed herein, for the purpose of developing the efficiency of operations, etc., provided such accounts do not impair the integrity of any accounts prescribed herein.

(D) As of the effective date of this system of accounts, the several accounts prescribed herein shall be opened by transferring thereto the balances carried in the accounts previously maintained by the company. The company is authorized to make such subdivisions, reclassifications, or consolidations of such balances as are necessary to meet the requirements of this system of accounts.

3. **Definitions.**—When used in this system of accounts:

(A) "Accounts" or "These accounts" means the accounts of this system of accounts.

(B) "Actually issued," as applied to certificates of capital stock or evidences of funded debt issued or assumed by the company, means those which have been sold to bona fide purchasers for a valuable consideration (including those issued in exchange for other securities or other property) under the condition that the purchasers secured them free from all control by the issuing company, also securities issued as dividends on stock.

(C) "Actually outstanding," as applied to certificates of capital stock or evidences of funded debt, means those which have been actually issued and are neither retired nor held by or for the company.

(D) "Affiliated companies" means:

(1) Controlled companies, i. e., companies solely controlled by the company, and also companies jointly controlled by the company and others under a joint arrangement.

(2) Controlling companies, i. e., companies solely controlling the company, and also companies which jointly control the company under a joint arrangement.

(3) Companies controlled by controlled companies.

(4) Companies controlled by controlling companies.

(*a*) By "control" is meant the ability to determine the action of a company. For the purposes of this instruction the following are to be considered forms of control:

(1) Right through title to securities issued or assumed to exercise the major part of the voting power in the controlled company.

(2) Right through agreement of some character or through some source other than title to securities to name the majority of the board of directors, managers, or trustees of the controlled company.

(3) Right to foreclose a first lien upon all or a major part in value of the tangible property of the controlled company.

(4) Right to secure control in consequence of advances made for construction of tangible property of the controlled company.

(5) Right to control only in a specific respect the action of the controlled company.

(*b*) A leasehold interest in the property of a company is not for the purpose of these accounts to be classed as a form of control over the lessor company.

(*c*) Sole control is that which rests in one company.

(*d*) Joint control is that which rests in two or more companies and which is held under a joint arrangement.

(E) "Book cost" means the amount at which property is recorded in these accounts.

(F) "Book liability" means the amount at which securities issued or assumed by the company and other liability items are recorded in these accounts.

(G) "Company" or "The company," when not otherwise indicated in the context, means the accounting company.

(H) "Cost of removal" means the cost of demolishing, dismantling, removing, tearing down, or otherwise disposing of telephone plant and recovering the salvage including the cost of transportation and handling incident thereto.

(I) "Debt expense," as applied to funded debt, means all expense in connection with the issue and sale of evidences of debt, such as fees for drafting mortgages and trust deeds; fees and taxes for issuing or recording evidences of debt; cost of engraving and printing bonds, certificates of indebtedness, and other commercial paper having a life of more than one year; fees paid trustees; specific costs of obtaining governmental authority; fees for legal services; fees and commissions paid underwriters, brokers, and salesmen for marketing such evidences of debt; fees and expense of listing on exchanges, and other like costs.

(J) "Depreciation," as applied to depreciable telephone plant, means the loss in service value (note instruction 3–Y) not restored by current maintenance, incurred in connection with the consumption or prospective retirement of telephone plant in the course of service from causes which are known to be in current operation, against which the company is not protected by insurance, and the effect of which can be forecast with a reasonable approach to accuracy.

(K) "Discount," as applied to securities issued or assumed by the company, means the excess of the par or face value of the securities plus interest or dividends accrued at the date of the sale over the current money value of the consideration received at their sale.

(L) "Group plan," as applied to depreciation accounting, means the plan under which depreciation charges are accrued upon the basis of the book cost of all property included in each depreciable account, using the average service life thereof properly weighted, and upon the retirement of any depreciable property its full service value is charged to the depreciation reserve whether or not the particular item has attained the average service life.

(M) "Investment advances," means advances, represented by notes or by book accounts only, with respect to which it is mutually agreed or intended between the creditor and the debtor that they shall be settled by the issuance of capital stock or funded debt or shall not be subject to current cash settlement.

(N) "Minor items," as applied to depreciable telephone plant, means any part or element which is not designated as a unit of property in Appendix A.

(O) "Miscellaneous physical property" means all physical property owned by the company other than telephone plant.

(P) "Net salvage value" means the salvage value (note instruction 3–W) of the property retired after deducting the cost of removal.

(Q) "Nominally issued," as applied to certificates of capital stock or evidences of funded debt, means those which have been

signed, certified or otherwise executed and placed with the proper officer for sale, or pledged or otherwise placed in some special fund of the company but which have not been sold,

(R) "Nominally outstanding," as applied to certificates of capital stock or evidences of funded debt, means those which after being actually issued have been reacquired by or for the company under such circumstances as require them to be considered as held alive and not retired.

(S) "Nonaffiliated companies" means all companies other than those defined as affiliated in instruction 3–D.

(T) "Plant retired" means plant which has been removed, sold, abandoned, destroyed, or otherwise withdrawn from telephone service, and not held for such service.

(U) "Premium," as applied to securities issued or assumed by the company, means the excess of the current money value of the consideration received at their sale over the sum of their par or face value and interest or dividends accrued at the date of the sale.

(V) "Replacing" and "replacement," when not otherwise indicated in the context, mean the construction or installation of telephone plant in place of plant retired together with the removal and recovery of the plant retired.

(W) "Salvage value" means the amount received for property retired, if sold, or if retained for reuse, the value at which the material recovered is chargeable to account 122, "Material and supplies."

(X) "Service life" means the period between the time of installation (note instruction 3–CC) of telephone plant and its time of retirement.

(Y) "Service value" means the difference between the book cost and:

(1) The salvage value (note instruction 3–W) for station apparatus.

(2) The net salvage value (note instruction 3–P) for other telephone plant.

(Z) "Straight-line method," as applied to depreciation accounting, means the plan under which the service value of property is charged to operating expenses and to clearing accounts and credited to the depreciation reserve through equal annual charges as nearly as may be during its service life.

(AA) "Telephone operations" and "telephone service" mean the service by common carriers of transmitting intelligence by wire or wireless primarily through the use of telephones, and services incidental or auxiliary to such service, such as private line, teletypewriter, telegraph, and telephotograph services.

(BB) "Telephone plant" means physical property used in telephone service and physical property held for such service under a definite plan.

(CC) "Time of installation" means the date at which telephone plant is completed ready for service.

(DD) "Time of retirement" means the date at which telephone plant is retired from telephone service.

4. **Unaudited items.**—When the amount of any known item affecting these accounts can not be accurately determined in time for inclusion in the accounts of the calendar year in which the transaction occurs, the amount of the item shall be estimated and included in the proper accounts. When the item is audited, the necessary adjustments shall be made through the accounts in which the estimate was recorded. If during the interval between the date of inclusion of the item in the accounts and the date on which it is audited, a substantial difference from the initial estimate is determined, appropriate adjustments shall be made in the current accounts to cover such difference. The company is not required to anticipate minor items which would not appreciably affect these accounts.

5. **Delayed items.**—(A) The term "delayed items" means items relating to transactions which occurred before the current calendar year. It includes adjustments of errors in the income, operating revenue, and operating expense accounts of prior years.

(B) Delayed items shall be charged or credited to the same accounts which should have been charged or credited if the items had been taken up or adjusted in the period to which they pertained. When the amount of a delayed item is relatively so large that its inclusion in the accounts for a single month would seriously distort those accounts, it may be distributed in equal amounts to the accounts for the current and remaining months of the calendar year.

(C) If the amount of any delayed item is relatively so large that its inclusion in the accounts for a single year would seriously distort those accounts, the company, if so authorized upon application to this Commission, may distribute to surplus so much of the amount as may be authorized. In requesting such authority, the company shall file with this Commission the full particulars concerning each such item and the reasons which, in its judgment, indicate the propriety of such accounting.

6. **Spreading of income, revenue, and expense items.**—When the amount of any unusual item includable in an income, operating revenue, or operating expense account for a single month is relatively so large that its inclusion in the accounts for that month would seriously distort those accounts, it may be included in account 139, "Other deferred debits," or account 174, "Other deferred credits," as appropriate, and distributed in equal amounts to the accounts for the current and remaining months of the calendar year.

7. **Profits and losses from foreign exchange.**—(A) Profits and losses from premiums and discounts on foreign exchange shall be included, so far as practicable, in the accounts appropriate for the transactions in connection with which such items arise. For

example, profits realized and losses suffered due to the difference in rates of exchange between the date that money is borrowed or loaned and the date of payment or collection shall be included in account 402, "Miscellaneous credits to surplus," or account 413, "Miscellaneous debits to surplus," as may be appropriate.

(B) Minor amounts of profits and losses on foreign exchange arising in the course of the company's telephone operations and impracticable of allocation to each specific transaction involved shall be included in account 526, "Other operating revenues," or account 675, "Other expenses," as may be appropriate.

8. **Interpretation of item lists.**—Lists of "items" appearing in the texts of the several accounts are given for the purpose of clearly indicating the application of the prescribed accounting in specific cases. The lists are not to be considered as comprising all the items includable in the several accounts, but merely as representative of them. On the other hand, the appearance of an item in a list warrants the inclusion of such item in the account concerned only when the text of the account also indicates inclusion, inasmuch as the same item frequently appears in more than one list. The proper entry in each instance must be determined by the texts of the accounts.

9. **Submission of questions.**—To the end that uniformity of accounting may be maintained, the company shall submit all questions of doubtful interpretation of the prescribed accounting to this Commission for consideration and decision.

Balance-sheet Accounts

10. **Purpose of balance-sheet accounts.**—The balance-sheet accounts (100 to 181, inclusive) are designed to show the assets, liabilities, capital stock, and surplus or deficit of the company.

11. **Current assets.**—(A) In the group of accounts designated as current assets (accounts 113 to 123, inclusive) there shall not be included any item the book cost of which is not reasonably assured, except that items of current character but of doubtful value may be written down and for record purposes carried in these accounts at a nominal value. If not thus written down, they shall be included in account 139, "Other deferred debits," at book cost or nominal value, or written off, as may be appropriate; but they shall not be so included at book cost unless there is a reasonable prospect of future substantial value.

(B) The amount of any item written off shall be included in account 530, "Uncollectible operating revenues—Dr.," account 323, "Miscellaneous income charges," account 413, "Miscellaneous debits to surplus," or other appropriate account.

12. **Book cost of securities owned.**—(A) Securities issued by others shall be recorded in these accounts at the time of purchase at the current money value of the consideration given therefor by the company. (See also paragraph (D) of account 313 and paragraph (B) of account 314.)

(B) The company is allowed the option of writing down such book cost in recognition of depreciation in the value of the securities. It shall write down to a nominal amount or write off if there is no reasonable prospect of future substantial value. The amount of such adjustment shall be debited to account 413, "Miscellaneous debits to surplus." The company shall maintain a complete record of the facts on which it bases such adjustment.

13. **Company securities owned.**—(A) The book cost (note instruction 3–E) of nominally issued (note instruction 3–Q) and nominally outstanding (note instruction 3–R) stocks and funded-debt securities issued or assumed by the company shall be shown in the short columns only of the balance-sheet statement of the company to this Commission. Such securities having a par value shall be so shown at their par value and for stocks having no par value there shall be shown the number of shares and any nominal value assigned thereto.

(B) The necessary adjustments for the difference between the book liability for securities reacquired and the amounts actually paid for them shall be included, when a debit, in account 413, "Miscellaneous debits to surplus," and when a credit in account 402, "Miscellaneous credits to surplus."

NOTE.—The book liability for nonpar stock reacquired shall be obtained by first ascertaining the amount of the liability in account 150, "Capital stock," for the particular class of stock before the reacquirement. In this amount shall be included the proceeds realized at the sale, the amount of any assessments against stockholders, the amounts transferred to account 150 from surplus, less any amount which has been distributed from account 150 to the stockholders in liquidation. The amount thus ascertained shall be prorated to the shares reacquired on the basis of the proportion that the reacquired shares bear to the total number of shares actually outstanding immediately prior to their reacquirement. (See also accounts 104, 105, 136, and 137.)

14. **Discount and premium on capital stock.**—(A) A separate discount and premium account shall be maintained to include both discounts suffered and premiums realized at the sale or resale of each particular class of par stock issued or assumed by the company. (Note instruction 3–K–U.)

(B) Appropriations of surplus at any time to extinguish all or any part of the debit balance in any particular discount and premium account shall be charged to account 413, "Miscellaneous debits to surplus," and credited to the appropriate discount and premium account.

(C) In case the company is permitted and elects to distribute all or any part of the credit balance in any particular discount and premium account to its stockholders, the amount thus distributed shall be charged to that account.

(D) Assessments against stockholders shall be credited to the discount and premium account for the particular class of capital stock so assessed, except that assessments with respect to nonpar stock shall be credited to account 150, "Capital stock."

(E) Except as provided in paragraphs (B), (C), and (D) of this instruction, the balance in each of these accounts shall be carried

until the reacquirement of the securities to which it relates, at which time (except under provisions of instruction 16) the proportion (based on the relation of the amount of stock reacquired to the total amount outstanding before its reacquirement) of the balance in the discount and premium account for the particular class of stock reacquired shall be closed to account 402, "Miscellaneous credits to surplus," or to account 413, "Miscellaneous debits to surplus," as may be appropriate.

(F) No discount on capital stock shall be included in any account as a part of the cost of acquiring any property, or as a part of the cost of operation.

(G) If the net of the balances in the discount and premium accounts for all classes of capital stock outstanding is a debit balance, the amount shall be included in the balance-sheet statement in account 134, "Discount on capital stock," and if a credit balance the amount shall be included in account 152, "Premium on capital stock."

15. **Discount, premium, and expense on funded debt.**—(A) A separate discount, premium, and debt expense account shall be maintained to include both discounts suffered and premiums realized, together with expenses incurred, at the sale or resale of each particular class of funded debt issued or assumed by the company. (Note instruction 3–I–K–U.)

(B) The company may extinguish at any time through charges to account 413, "Miscellaneous debits to surplus," all or any part of the debit balance remaining in any particular discount, premium, and debt expense account.

(C) Each month or other accounting period there shall be credited to each particular discount, premium, and debt expense account in which there is a debit balance the proportion (based upon the ratio of the period to the life of the security remaining at the beginning of each such accounting period) of such debit balance as is applicable to the period. The amounts thus credited shall be concurrently charged to account 338, "Amortization of discount on funded debt." (See also instruction 22–B–10–*b*.)

(D) Correspondingly each month or other accounting period there shall be charged to each particular discount, premium, and debt expense account in which there is a credit balance the proportion of such credit balance as is applicable to the period. The amounts thus charged shall be concurrently credited to account 339, "Release of premium on funded debt—Cr." (See also instruction 22–B–10–*b*.)

(E) Except as provided in paragraphs (B), (C), and (D) of this instruction, the balance in each of these accounts shall be carried until the reacquirement of the securities to which it relates, at which time (except under provisions of instruction 16) the proportion (based on the relation of the amount of funded debt reacquired to the total outstanding before its reacquirement) of the

balance in the discount, premium, and debt expense account for the particular class of funded debt reacquired shall be closed to account 402, "Miscellaneous credits to surplus," or account 413, "Miscellaneous debits to surplus," as may be appropriate.

(F) No discount, premium, or expense on funded debt shall be included in any account as a part of the cost of acquiring any property or as a part of the cost of operation except under the provisions of instruction 22–B–10–*b*.

(G) If the net of the balances in the discount, premium, and debt expense accounts for all classes of funded debt outstanding is a debit balance, the amount shall be included in the balance-sheet statement in account 135, "Discount on funded debt," and if a credit balance the amount shall be included in account 168, "Premium on funded debt."

16. **Exchange of securities.**—Before recording journal entries which it is proposed to spread upon the company's books to record the reacquirement of capital stock or funded-debt securities issued or assumed by the company under a plan for the issuance in exchange therefor of the company's capital stock and/or funded-debt securities, a statement indicating the plan of accounting proposed by the company shall be presented to this Commission for consideration. Such statement shall give complete information concerning the plan of exchange; the authority of the regulatory body with respect thereto, if any; and the basis upon which the amounts have been determined.

17. **Contingent assets and liabilities.**—Contingent assets represent a possible source of value to the company contingent upon the fulfillment of conditions regarded as uncertain. Contingent liabilities include items which may under certain conditions become obligations of the company but which are neither direct nor assumed liabilities on the date of the balance sheet. In the annual report to this Commission contingent assets and contingent liabilities shall not be included in the balance sheet but contingent assets and liabilities shall be shown in detail in a supplementary statement accompanying it.

Telephone Plant Accounts

20. **Purpose of telephone plant accounts.**—(A) The telephone plant accounts (201 to 280, inclusive) are designed to show the cost of the company's telephone plant (note instruction 3–BB) which ordinarily has a service life of more than one year, including such plant whether used by the company or others in telephone service (note instruction 3–AA) and plant for which there is a definite plan for use in telephone service; also the cost of franchises, patents, rights of way, leaseholds, and other interests in land, undistributed cost of property and the general expenses of organization.

(B) Amounts chargeable to these accounts, except as provided in paragraph (C) in this instruction and instruction 21, shall be the actual money costs to the company of the property. When the consideration given for property is anything other than money the current money value of such consideration shall be used. The company shall be prepared to furnish this Commission the particulars of its determination of the money value of the consideration if other than money. (See also instructions 21, 22, 23, and 50–B–2.)

(C) Telephone plant donated to the company or constructed by it through expenditures of donations of money or its equivalent shall be charged to the telephone plant accounts at its estimated current cost new and there shall be credited to the depreciation reserve and amortization reserve accounts the estimated amount of the reserve requirements applicable to the plant. The difference between the amounts so includable in the telephone plant and the reserve accounts shall be credited to account 175, "Donations."

NOTE.—Amounts received for construction which are ultimately to be repaid, wholly or in part, shall be credited to account 174; when final determination has been made as to the amount to be returned any unrefunded amounts shall be credited to account 175.

(D) When property ordinarily having a service life of more than one year is installed for temporary use in telephone service it shall be accounted for in the same manner as telephone plant having a service life of more than one year. This includes temporary installations of station equipment, plant (such as poles, wire, and cable) installed to maintain service during the progress of highway reconstruction or during interruptions due to storms or other casualties, equipment used for the training of operators, equipment used to provide intercepting positions in central offices to handle traffic for a short period following cut over to dial-system service, and similar installations of property for telephone service.

(E) The cost of individual items of equipment such as tools and office equipment of small value (for example, costing $10 or less) or short life shall be charged to the appropriate operating expense or clearing accounts according to the use of such items, except that such accounting shall not be permitted when the investment in such property is relatively large and the correctness of the accounting therefor is verified by current inventories.

21. **Telephone plant purchased.**—(A) When property in use in telephone service (note instruction 3–AA) is purchased, the accounting therefor shall be as follows:

(B) There shall be charged as of the date of purchase:

(1) To account 211, "Land," the estimated current value of the land.

(2) To the depreciable plant accounts, the current cost new (estimated if not known), of the property classable therein.

(3) To account 202, "Franchises," the original cost of all governmental franchises and similar rights acquired.

(4) To accounts 232, "Station installations," and 233, "Drop and block wires," such proportion of the estimated current cost

new, of the plant includable in each of these accounts as the estimated remaining service life of the respective classes of plant includable therein bears to the average over-all service life of the same class of plant installed by the accounting company.

(5) To account 280, "Construction work in progress," the cost of any uncompleted projects acquired.

(C) The estimated amount of the reserve requirements applicable to the plant shall be credited to accounts 171, "Depreciation reserve," and 172, "Amortization reserve."

(D) The difference between the net of the amounts includable in these accounts as provided in the foregoing paragraphs B and C and the cost to the accounting company of the plant purchased shall be debited or credited as appropriate to account 278, "Undistributed cost of property," except that when any difference thus chargeable to account 278 applies to duplicate or other telephone plant which will be retired by the purchaser in the reconstruction of the purchased property and its consolidation with previously owned property, the accounting for the amount applicable to such plant shall be presented to this Commission for consideration and approval.

(E) Upon application by the company, in each instance, to this Commission and subject to its approval, the company may charge to its telephone plant accounts and may also credit to its depreciation and amortization reserve accounts the amounts carried in those accounts by the vendor company with respect to the property purchased.

(F) Journal entries recording the purchase of a complete telephone system, a complete exchange or a complete toll system, shall be presented to this Commission for consideration and approval. The text of such entries shall give a complete description of the property purchased and the bases upon which the amounts of the entries have been determined.

22. **Cost of construction.**—(A) The cost of the construction of property chargeable to the telephone plant accounts shall include the cost of labor, material and supplies, transportation, contract work, protection, injuries and damages, privileges and permits, taxes, rent, interest during construction, insurance, and other analogous elements in connection with such work. (See also instruction 20–B.)

(B) The following is a description of the major items referred to in the foregoing paragraph:

(1) "Cost of labor" includes the pay and expenses of employees directly engaged in or being trained for construction work, of foremen in direct charge thereof, and an equitable proportion of the cost of local plant administration, general plant supervision and engineering, and of the pay, office, and other expenses of general officers and general office employees devoting part of their time to supervisory, administrative, or clerical functions in connection with construction work.

(2) "Cost of material and supplies" includes the purchase price at the point of free delivery plus the costs of inspection, loading and transportation, and an equitable proportion of supply expense. In determining the cost of material used, proper allowance shall be made for unused material, for material recovered from temporary structures used in performing the work involved, and for discounts allowed and realized in the purchase of material.

(3) "Cost of transportation" includes the cost of transporting employees, material and supplies, tools, and other work equipment. It includes amounts paid therefor to other companies or individuals and the cost of the company's own motor vehicle or other transportation service.

(4) "Cost of contract work" includes amounts paid for work performed under contract by other companies, firms, or individuals, engineering and supervision applicable to such work, costs incident to the award of contracts and the inspection of such work.

(5) "Cost of protection" includes the cost of protecting the company's property from fire or other casualties and the cost of preventing damages to others or the property of others.

(6) "Cost of injuries and damages" includes expenditures or losses in connection with construction work on account of injuries to persons (other than payments to or on behalf of employees made under a company's general provision for employees' benefits—see account 672) and on account of damages to the property of others. (See also account 669.)

(7) "Cost of privileges and permits" includes payments for and expenses incurred in securing privileges, permits, or rights in connection with construction work, such as for use of private property, streets, or highways. The cost of such privileges and permits shall be included in the cost of the work for which the privileges or permits are secured, except for costs includable in account 202, "Franchises," and account 207, "Right of way."

(8) "Taxes" includes taxes on physical property during construction and before the facilities are completed ready for service. This includes taxes on land held under a definite plan for its use in telephone service for the period prior to the completion of telephone facilities thereon and other taxes assessed on property during construction, separately from taxes on operating property or assessed under conditions which permit separate identification or allocation of the amount chargeable to construction.

(9) "Rent" includes payments for the use of facilities, such as motor vehicles, special tools or machines, and quarters used in construction work.

(10) "Interest during construction" includes the amount of interest upon all moneys, including the company's own funds, used in the acquisition or construction of telephone property and shall

be charged to the accounts appropriate for the cost of the property acquired or constructed as follows:

(a) Reasonable amounts for interest during the construction period (before the property is received or is completed ready for telephone serivce) on general funds expended for the acquisition or construction of telephone plant shall be charged to the telephone plant accounts and credited to account 313, "Interest income."

(b) When funds, derived from the sale of bonds, notes, and other interest-bearing debt, are specifically acquired and separately held for use in the construction of telephone plant, the total interest, discount or premium, and expense on such debt applicable to the accounting period shall be included in the cost of telephone plant and credited to account 313, "Interest income."

(c) During a period of suspension of a construction project no interest charge for a longer period than one year from the date of its suspension shall be included in these accounts unless specifically authorized by this Commission. No such interest charges shall be included in these accounts on expenditures for construction projects which have been definitely abandoned.

(11) "Insurance" includes premiums paid or amounts credited to account 169 for the protection against loss and damages in connection with the construction of telephone plant due to fire or other casualty, injury to or death of employees or others, damages to property of others, defalcation of employees and agents, and the nonperformance of contractual obligations of others. (See also account 668.)

23. **Improvements to leased telephone plant.**—(A) Except as provided in paragraph (B) following, the cost of initial improvements (including repairs, rearrangements, additions, and betterments) to telephone plant leased from others made in the course of preparing the property for service and the cost of any subsequent additions and betterments of the leased telephone plant shall be charged to the telephone plant account appropriate for the class of property leased, unless the leasing arrangements provide that specific improvements shall be made to the leased property by the lessee and that such improvements shall revert to the lessor and constitute a part of the consideration paid for the use of the property. In the latter case, the cost of the improvements reverting to the lessor which represents payments for the use of the lessor's property shall be charged to account 129, "Prepaid rents," and cleared over the period of the lease to the appropriate rent expense or clearing accounts.

(B) When the improvements to leased telephone plant otherwise chargeable to the telephone plant accounts are of relatively minor cost or short life or the period of the lease is less than one year, the cost shall be charged to the account chargeable with the cost of repairs of such plant.

(C) When the cost of improvements to leased telephone plant is included in the telephone plant accounts, charges for depreciation thereof shall be made on such basis as will amortize the service value of such improvements during the period of their expected use.

24. **Units of property.**—The "units of property" (see also instruction 25–A–1) established at the date of issuance of this system of accounts are listed in Appendix A. Additions to or revisions of this list will be issued, when necessary, by this Commission, to which any applications for such additions or revisions shall be presented by the company.

25. **Telephone plant retired.**—(A) Depreciable telephone plant: For the purpose of avoiding undue refinement in accounting for the replacement of small items of property, the accounting for retirements and replacements of depreciable telephone plant, as grouped below, shall be as follows:

(1) *Units of property.*—This group includes major items of property, a list of which is shown in Appendix A. The book cost of any such item retired shall be credited to the plant account and charged to account 171, "Depreciation reserve," whether or not replaced. (See also par. (B) of the text of account 171.) The cost of property installed in place of the property retired shall be charged to the appropriate telephone plant account.

(2) *Minor items.*—This group includes any part or element which is not designated as a unit of property. The book cost of any minor item of property retired and not replaced shall be credited to the plant account and charged to account 171 (see also par. (B) of the text of that account), except that if the book cost of a minor item of property is accounted for through the retirement of units of property, no separate credit to the telephone plant account is required when such an item is retired. Except as provided in note under account 231, "Station apparatus," in Appendix A, if minor items of property are retired and replaced (apart from the unit of property of which they form a part or with which they are associated) no adjustment shall be made in account 171. The cost of the replacement shall be charged to the account appropriate for the cost of repairs of the property, except that if the replacement effects a substantial betterment (the primary aim of which is to make the property affected more useful, of greater durability or of greater capacity) the excess cost of the replacement over the estimated cost at current prices of replacing without betterment the minor items retired shall be charged to the appropriate telephone plant account.

(B) Station installations, drop and block wires: When stations are removed from customers' premises the book cost of the station installations carried in account 232, "Station installations," and of any drop and block wires carried in account 233, "Drop and block wires," thereby retired from service shall be credited to the plant

accounts and charged to account 607, "Station removals and changes." The latter account shall be credited with the salvage value (note instruction 3–W) of such property recovered. The cost of the removal of the station apparatus, inside, drop and block wires shall be charged to account 607.

(C) Land: The book cost of land retired shall be credited to account 211, "Land." If the land is sold, the difference between such book cost and the sale price (less commissions and other expenses of making the sale) of the land shall be credited to account 401, "Credits for telephone plant sold," or debited to account 410, "Debits for telephone plant sold," as may be appropriate. If the land is retained by the company and held other than for immediate sale, the book cost shall be charged to account 103, "Miscellaneous physical property." The accounting for leaseholds retired shall be as provided for in the texts of account 172, "Amortization reserve," and account 671, "Operating rents."

(D) Determination of book costs: The book cost of telephone plant retired shall be the amount at which such property is included in the telephone plant accounts when such amount can be determined from the company's records. Ordinarily, such records shall be used in the retirement of land, buildings, complete central offices, furniture and other items of plant for which individual cost records are maintained. When the actual book cost can not be determined from the records, it shall be estimated. When it is impracticable to determine the book cost of each item due to the relatively large number or small cost of such items, the average book cost of all the items shall be used in determining the book cost of the items retired. The latter method may be applied in retirement of such items as telephones, bell boxes, station installations, poles, cross arms, wire, cable, cable terminals, conduit, and non-multiple private branch exchange switchboards.

(E) The accounting for the retirement of Organization, Franchises, Patent rights and Undistributed cost of property, shall be as provided in the texts of account 172, "Amortization reserve," account 413, "Miscellaneous debits to surplus," account 673, "Telephone franchise requirements," and account 675, "Other expenses."

(F) When telephone plant is sold together with the telephone traffic associated therewith, the book cost of the property shall be credited to the appropriate plant accounts and the estimated amounts carried with respect thereto in the depreciation and amortization reserve accounts shall be charged to such reserve accounts. The difference, if any, between (a) the net amount of such debit and credit items and (b) the consideration received (less commissions and other expenses of making the sale) for the property shall be included, if a debit, in account 410, "Debits for telephone plant sold," and if a credit, in account 401, "Credits for telephone plant sold." The accounting for depreciable telephone

plant sold without the traffic associated therewith shall be in accordance with the accounting provided in paragraph (B) of account 171, "Depreciation reserve."

Income Accounts

30. **Purpose of income accounts.**—The income accounts (300 to 344, inclusive) are designed to show as nearly as practicable for each calendar year, the total operating revenues and operating expenses of the company; the returns accrued upon securities owned and from property not used in the company's operations; the amounts accrued for taxes, use of moneys, and use of operating properties of others; and reservations and appropriations of income. (See also instructions 4, 5, and 6.)

31. **Income from sinking and other funds.**—When interest and other income arising from funds carried in account 104, "Sinking funds," account 136, "Provident funds," or account 137, "Insurance and other funds," (see also account 314) are required by the mortgage or other provisions to be held in the funds, they shall be charged to those accounts. If such funds are represented by a reserve established through reservations of income or surplus, amounts so set aside shall be charged to account 342, "Contractual reservations of income," account 343, "Miscellaneous reservations of income," account 414, "Contractual reservations of surplus," or account 415, "Miscellaneous reservations of surplus," and credited to account 169, "Insurance reserve," account 170, "Provident reserve," or account 180, "Surplus reserved," as may be appropriate.

Surplus Accounts

40. **Purpose of surplus accounts.**—The surplus accounts (400 to 416, inclusive) are designed to show the changes in the company's surplus or deficit during each calendar year resulting from (*a*) the operations and other transactions during that period reflected in the income accounts, (*b*) appropriations or other reservations of surplus for specific purposes, (*c*) accounting adjustments not properly attributable to the period (see also instruction 5) and (*d*) miscellaneous losses and gains not provided for elsewhere. The balance of the surplus accounts (400 to 416, inclusive) shall be closed into account 181, "Unappropriated surplus," at the end of each calendar year.

Operating Revenue Accounts

50. **Purpose of operating revenue accounts.**—(A) The operating revenue accounts (500 to 530, inclusive) are designed to show the amounts of money which the company becomes lawfully entitled to receive from the furnishing of telephone service (including operations incidental thereto). Credits to the various revenue accounts shall be based upon the actual amounts chargeable for services rendered by the company. It is not required that

undetermined amounts of revenue at pay stations lost through fire, theft, or collection of slugs or coins having no legal tender value shall be included in the operating revenue accounts. (See also instructions 4, 5 and 6 and account 650.)

(B) In addition to monthly service charges, the operating revenue accounts appropriate for the class of service involved shall be credited with:

(1) Amounts charged for connection, restoration and termination of service and for inside moves, outside moves, instrument changes and similar service requirements.

(2) Amounts of initial nonrecurring charges for special or auxiliary plant or equipment furnished in rendering service to a customer, except that charges for the cost of providing plant or equipment the ownership of which rests with or will revert to the customer shall be credited to the accounts charged with the cost of such plant or equipment.

(3) Amounts of service charges for supplemental or auxiliary equipment furnished in rendering service to a customer—for example, extension stations, auxiliary receivers, auxiliary signals, code calling and conference equipment, etc.

(C) The classification of operating revenues provides separate accounts for local revenue and for toll revenue. In case it is necessary to apportion the revenue between these accounts, the company shall be prepared when so required by this commission to furnish the basis used in making such apportionment.

51. **Deductions from revenues.**—Discounts allowed customers for prompt payment, corrections of overcharges, authorized refunds of overcollections theretofore credited, authorized refunds and adjustments on account of failures in service, and other corrections shall be charged to the revenue account previously credited with the amounts involved.

52. **Commissions.**—(A) Commissions paid to employees or others in place of salaries or other compensation for services rendered, such as public telephone commissions, shall be charged to the appropriate expense accounts and not to the revenue accounts.

(B) Originating and other commissions representing divisions of operating revenues between telephone companies shall be accounted for through the appropriate operating revenue accounts.

Operating Expense Accounts

60. **Purpose of operating expense accounts.**—The operating expense accounts (602 to 677, inclusive) are designed to show the expenses of furnishing telephone service (note instruction 3–AA) including expense of maintaining the plant used in such service. (See also instructions 4, 5, and 6.)

61. **Cost of repairs.**—(A) The cost of repairs chargeable to the various operating expense and clearing accounts includes: Inspect-

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ing, testing, and reporting on the condition of telephone plant to determine the need for repairs, replacements, rearrangements, and changes; testing for, locating and clearing trouble; routine work (see also par. B) to prevent trouble, such as pulling up slack, tightening guys and raking guy stubs, trimming trees, straightening poles and cross arms and cleaning and adjusting equipment; replacing minor items of telephone plant (see also instruction 25); rearranging and changing the location of property not retired; repairing material for reuse; restoring the condition of property damaged by storms, floods, fire, or other casualties (see also par. B); training employees for maintenance work; inspecting and testing after repairs have been made; and an equitable proportion of the cost of local plant administration, general plant supervision and engineering.

(B) The cost of repairs does not include the cost of replacing items of property designated as "units of property" except as provided in account 605, "Repairs of station equipment," for labor and incidental costs in the replacement of station apparatus. (See also instruction 25.)

62. **Joint operating expenses.**—(A) In accounting for operating expenses incurred under arrangements for joint participation or apportionment between telephone companies, the creditor company shall charge initially the entire expense to the appropriate primary accounts. The proportion of such expenses borne by the debtor shall be credited by the creditor and charged by the debtor to the accounts initially charged, except that by agreement between the participating companies the proportion of traffic expenses borne by the debtor may be credited by the creditor to account 635, "Joint traffic expenses—Cr.," and charged by the debtor to account 634, "Joint traffic expenses—Dr."

(B) Any allowances for return on the property used under the arrangement shall be credited by the creditor to the appropriate rent revenue account and charged by the debtor to the appropriate rent expense account.

(C) The creditor company shall inform the debtor company of the distribution of charges made by it.

63. **Distribution of pay and expenses of employees.**—(A) Charges to the telephone plant, operating expense and other accounts for services and expenses of employees engaged in activities chargeable to various accounts shall be based upon the actual time engaged in the respective classes of work, except that the pay and expenses of an employee who performs the same class of work from day to day may be distributed upon the basis of a study of the time actually engaged during a representative period.

(B) The pay and expenses of employees of one department who perform for another department incidental services involving only small expense shall be included in the expenses of the department in which the employees are regularly employed.

64. **Extensive replacements.**—When it becomes necessary to replace the majority of either station apparatus, inside, drop, or block wires, in any given central office district, together with any number of such items in contiguous districts, the cost of the replacements chargeable to account 605, "Repairs of station equipment," if so authorized by this Commission upon application to it, shall be charged to account 138, "Extraordinary maintenance suspense," and cleared to account 605, "Repairs of station equipment," over the period specified in the authority.

Clearing Accounts

70. **Purpose of clearing accounts.**—The clearing accounts (702 to 707, inclusive) are designed to facilitate the distribution of certain items which usually affect both construction and other operations. Any such items which can be properly allocated to the appropriate primary accounts as they are incurred may be charged direct to those accounts. (See also instruction 2–C.)

Depreciation Accounting

80. **Computation and filing of depreciation rates.**—(A) The company shall file with the State commission or commissions having jurisdiction, for review and recommendations to this Commission, estimates of the composite annual percentage rates considered applicable to the book cost of each class of depreciable telephone plant owned or used by the company. These percentage rates shall be based upon the estimated service values and service lives developed by a study of the company's history and experience and such engineering and other information as may be available with respect to prospective future conditions. These percentage rates shall be computed in conformity with the group plan of accounting for depreciation and shall be such that the loss in service value of the property, except for losses excluded under the definition of depreciation (note instruction 3–J), may be distributed under the straight-line method (note instruction 3–Z) during the service life of the property. Such percentage rates shall for each primary account comprised of more than one class of property produce a charge to operating expenses for that account equal to the sum of the amounts that would otherwise be chargeable for each of the various classes of property included in the account. The estimates of the composite annual percentage rates so filed shall be accompanied by a sworn statement showing the bases therefor and the methods employed in their computation. Where no State commission has jurisdiction or is willing to act in the premises, the estimates and the accompanying statement shall be filed with this Commission. A company subject to the provisions of this system of accounts January 1, 1933, shall file such estimates not later than August 1, 1933. A company which becomes subject to the pro-

visions of this system of accounts after January 1, 1933, shall file such estimates within six months after the provisions of this system of accounts become applicable to it. After consideration of the recommendations of the State commission or commissions to the extent available, this Commission will by temporary order prescribe the composite annual percentage rates which shall be charged with respect to each class of depreciable telephone plant. After the issuance of the temporary order, opportunity will be afforded at public hearings, if desired, for the presentation of evidence by all interested parties with a view to the modification of such order and for the submission of views based on such evidence. Such public hearings shall be conducted for this Commission, so far as possible, by State commissions. The company shall be prepared at any time upon direction of this Commission to compute and submit, for its approval, revised percentage rates in cases where existing rates are deemed inapplicable.

(B) In the event any composite percentage rate prescribed by this Commission, in the judgment of the company becomes no longer currently applicable, the company shall in a like manner file estimates of revised composite annual percentage rates which, in its judgment, should be established.

(C) The company shall keep such records of property and property retirements as will reflect the service life of property which has been retired, or will permit the determination of service-life indications by mortality, turnover, or other appropriate methods, and also such records as will reflect the percentage of salvage value, or net salvage value, as appropriate, for property retired from each class of depreciable telephone plant.

81. **Depreciation charges.**—(A) Charges for currently accruing depreciation shall be made monthly to account 608, "Depreciation," and account 702, "Vehicle and other work equipment expense," as appropriate, and corresponding credits shall be made to account 171, "Depreciation reserve." In computing the current monthly charges, one-twelfth of the composite annual percentage rate applicable to the primary accounts covering depreciable telephone plant shall be applied to the average of the balances, as of the first and last of the current month, in each such primary account.

(B) In addition, when the company is responsible under the terms of a lease for depreciation of property, used but not owned, for which the rent is chargeable to account 303, "Rent for lease of operating property," depreciation charges shall be made on the same basis as for owned depreciable property.

(C) A separate composite annual percentage rate for each account covering depreciable telephone plant shall be used in computing depreciation charges. Such composite rates shall be those which are from time to time prescribed by this Commission, except that where no rates previously have been prescribed for the company's use by this Commission, the company's estimates of

composite annual percentage rates computed in accordance with instruction 80 shall be used prior to the date rates prescribed by this Commission become effective.

82. **Classes of depreciable telephone plant.**—The classes of depreciable telephone plant and the accounts covering such plant are as follows:

Right of way (account 207).
Buildings (account 212).
Central-office equipment (account 221).
Station apparatus (account 231).
Private branch exchanges (account 234).
Booths and special fittings (account 235).
Pole lines (account 241).
Cable (account 242).
Aerial wire (account 243).
Underground conduit (account 244).
Furniture and office equipment (account 261).
Vehicles and other work equipment (account 264).

83. **Plant retired for causes not factors in depreciation.**—The service value of depreciable telephone plant retired (see also instruction 25) shall be charged in its entirety to account 171, "Depreciation reserve." If the cause of retirement is not a recognized factor in depreciation (note instruction 3-J) and the loss is not covered by insurance, the company may, upon proof that the charge to the depreciation reserve will result in undue depletion thereof, and with the approval of this Commission, credit account 171, "Depreciation reserve," and charge account 138, "Extraordinary maintenance suspense," with the unprovided-for loss in service value and distribute it from that account to account 609, "Extraordinary retirements," over such period as this Commission may approve.

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BALANCE SHEET ACCOUNTS

(Note particularly instructions 10 to 17, inclusive)

I. Investments

100. Telephone plant.—This account shall include the company's investment in property used or held under a definite plan for telephone service (note instruction 3–AA) at the date of the balance sheet as classified under accounts 201 to 280, inclusive. (See also instructions 2–C, 20 and 21.)

101. Investments in affiliated companies.—(A) This account shall include the book cost (see also instruction 12) of the company's investment in securities issued or assumed by affiliated companies (note instruction 3–D) other than securities held in special funds (see also note C to this account) or as temporary cash investments, and also its investment advances (note instruction 3–M) to such companies.

(B) This account shall be maintained to show separately the book cost of:

(1) Stocks.
(2) Funded debt.
(3) Investment advances.

(C) The company's records shall be kept in such manner that in the annual report to this Commission the securities pledged as collateral security for any of the company's funded debt or short-term loans or to secure performance of contracts may be shown separately from securities unpledged.

Note A.—Amounts receivable from affiliated companies which are subject to current settlement shall be included in account 120.

Note B.—The value of securities borrowed by the company shall not be included in this account.

Note C.—The book cost of securities held in special funds shall be included in accounts 104, 136, or 137, as may be appropriate.

Note D.—Working funds advanced to affiliated companies other than investment advances (note instruction 3–M) shall be included in account 115.

102. Other investments.—(A) This account shall include the book cost (see also instruction 12) of the company's investment in securities issued or assumed by nonaffiliated companies (note instruction 3–S) and individuals, other than securities held in special funds (see also note C to this account) or as temporary cash investments; also its investment advances (note instruction 3–M) to such parties and special deposits of cash for more than one year from date of deposit.

(B) This account shall be maintained to show separately the book cost of:

(1) Stocks.
(2) Funded debt.
(3) Investment advances.
(4) Special deposits of cash for more than one year from date of deposit.

(C) The company's records shall be kept in such manner that in the annual report to this Commission the securities pledged as collateral security for any of the company's funded debt or short-term loans or to secure the performance of contracts may be shown separately from the securities unpledged.

NOTE A.—Amounts receivable from nonaffiliated companies and individuals which are subject to current settlement shall be included in account 120.

NOTE B.—The value of securities borrowed by the company shall not be included in this account.

NOTE C.—The book cost of securities held in special funds shall be included in accounts 104, 136, or 137, as may be appropriate.

NOTE D.—Working funds advanced to nonaffiliated companies and individuals other than investment advances (note instruction 3–M) shall be included in account 115.

103. Miscellaneous physical property.—This account shall include the company's investment in physical property other than telephone plant (the investment in which is includable in account 100). It shall include the cost of land when acquired other than that for which there is a definite plan for its use in telephone service and buildings and other improvements upon such land; also the cost of land retired from telephone service and held other than for immediate sale, and buildings and other improvements upon such land. It shall include also the company's investment in property, such as lighting, water, power, and manufacturing plants, not held incident to the company's telephone operations, and assessments against miscellaneous physical property for the construction of public improvements.

NOTE.—The cost of land or buildings retired from telephone service and held for immediate sale shall be carried in account 211 or 212, respectively.

104. Sinking funds.—(A) This account shall include the amount of cash, the book cost of securities issued by other companies and of nominally issued and nominally outstanding (note instruction 3–Q–R) securities issued or assumed by the company, and other assets which are held by trustees or by the company's treasurer in a distinct fund, for the purpose of redeeming outstanding obligations. (See also instructions 12, 13, and 31.)

(B) A separate account shall be kept for each sinking fund under a title which shall designate the obligation in support of which the fund was created.

105. Company securities owned.—(A) This account shall include the book cost of nominally issued and nominally outstanding (note instruction 3–Q–R) securities issued or assumed by the

company, other than such securities held in sinking or other special funds. (See also instruction 13.)

(B) This account shall be maintained to show:

(1) For stock—

(a) Par stock.

(1) Number of shares and total par value of shares unpledged.

(2) Number of shares and total par value of shares pledged.

(b) Nonpar stock—

(1) Number of shares and any nominal value assigned to shares unpledged.

(2) Number of shares and any nominal value assigned to shares pledged.

(2) For funded debt—

(a) Total par value unpledged.

(b) Total par value pledged.

II. Current Assets

113. Cash.—This account shall include the amount of current funds available for use on demand in the hands of financial officers and agents, or deposited in banks or with trust companies, also funds in transit for which agents have received credit. (See also instruction 11.)

Note.—Working funds shall be included in account 115.

114. Special cash deposits.—This account shall include the amount of cash on special deposit, other than in sinking and other special funds provided for elsewhere, to pay dividends, interest, and other debts, when such payments are due one year or less from the date of deposit; the amount of cash deposited to insure the performance of contracts to be performed within one year from date of the deposit; and other cash deposits of a special nature not provided for elsewhere. This account shall include the amount of cash deposited with trustees to be held until mortgaged property sold, destroyed, or otherwise disposed of is replaced, and also cash realized from the sale of the company's securities and deposited with trustees to be held until invested in physical property of the company or for disbursement when the purposes for which the securities were sold are accomplished. (See also instruction 11.)

Note A.—Cash on deposit in special accounts where the funds are available for the current requirements of the company shall be included in account 113.

Note B.—This account shall not include any amounts representing securities owned.

Note C.—Cash on special deposit to be held for more than one year from the date of deposit shall be included in account 102.

115. Working funds.—This account shall include amounts advanced to officers, employees, and others as working funds from which certain expenditures are to be made and accounted for. (See also instruction 11.)

116. **Temporary cash investments.**—This account shall include the book cost of securities acquired for the purpose of temporarily investing cash, such as time drafts receivable and time loans, bankers' acceptances, United States Treasury certificates, marketable securities, and other similar investments of a temporary character. (See also instructions 11, 12, and 13.)

117. **Notes receivable.**—This account shall include the book cost not includable elsewhere, of all collectible obligations in the form of notes receivable and other similar evidences (except interest coupons) of money receivable on demand or within a time not exceeding one year from date of issue. (See also instruction 11.)

NOTE.—Obligations any part of which matures more than one year from date of issue, obligations maturing serially any part of which matures more than one year from date of issue, and notes evidencing investment advances (note instruction 3-M) are includable in accounts 101, 102, 104, 116, 136 or 137.

118. **Due from customers and agents.**—This account shall be subdivided as follows:

(A) Due from customers and agents.

(1) This subaccount shall include amounts due from customers for services rendered or billed and from agents and collectors authorized to make collections from customers (see also instruction 11). This subaccount shall be kept in such manner as will enable the companies to make the following analysis:

(*a*) Amounts due from customers who are still receiving telephone service.

(*b*) Amounts due from customers whose telephone service has been discontinued and whose accounts are in process of collection.

(2) Collections in excess of amounts charged to this subaccount may be credited to and carried in this account until applied against charges for services rendered or until refunded.

(3) The amount of notes held as security for customers' accounts may be carried in this account pending collection.

(B) Reserve for uncollectible accounts—Cr.

(1) This subaccount shall be credited with such amounts as may be charged to account 530, "Uncollectible operating revenues—Dr.," to provide for uncollectible accounts included in subaccount 118–A. (See also instruction 51.) There shall also be credited to this subaccount amounts collected which previously have been written off through charges to this subaccount and credits to subaccounts 118–A.

(2) If this reserve for uncollectible accounts is maintained, to it shall be charged any amounts covered thereby which have been found to be impracticable of collection. If such reserve is not maintained, amounts included in subaccount 118–A which have been found to be uncollectible shall be charged to account 530, "Uncollectible operating revenues—Dr."

120. **Accounts receivable.**—(A) This account shall include amounts currently due from others and not provided for in other

accounts, such as those for traffic settlements, material and supplies, repairs to telephone plant, matured rents, and interest receivable under monthly settlements on short-term loans, advances and open accounts. (See also instruction 11.)

(B) In the balance sheet statement there may be included in this account the net amount receivable from companies against each of which there is a net debit balance between this account and account 159, "Accounts payable."

121. **Interest and dividends receivable.**—This account shall include the amount of interest accrued to the date of the balance sheet on bonds, notes and other commercial paper owned, on loans made and the amount of dividends receivable on stocks owned. (See also instruction 11.)

NOTE A.—These accounts (note instruction 3-A) shall not include dividends or other returns on securities issued or assumed by the company and held by or for it, whether pledged as collateral, or held in its treasury, in special deposits or in sinking and other funds.

NOTE B.—Interest receivable under monthly settlements on short-term loans, advances, and open accounts, shall be included in account 120.

122. **Material and supplies.**—(A) This account shall include the cost of unapplied material and supplies held in stock, including plant supplies, tools, fuel, stationery, directory paper stock, and other supplies, and articles in process of manufacture for supply stock.

(B) Transportation charges, so far as practicable, shall be included as a part of the cost of the particular material to which they relate. When not so includable, they shall be charged to account 704, "Supply expense."

(C) So far as practicable, cash and other discounts on material shall be deducted in determining the cost of the particular material to which they relate or credited to the account to which the material is charged. When not so deductible, they shall be charged to account 704, "Supply expense."

(D) Material recovered in connection with construction, maintenance, or the retirement of property shall be charged to this account as follows (note instruction 3–W):

(1) Reusable material consisting of large individual items such as central office and multiple branch exchange switchboards shall be included in this account on the basis of book cost, estimated if not known. The cost of repairing such items shall be charged to the appropriate account in operating expenses.

(2) Reusable material consisting of relatively small items such as those the identity and original cost of which can not be maintained (from date of original installation in plant to the final abandonment or sale thereof) without excessive cost of handling and undue refinement in accounting shall be included in this account upon the basis of current prices new for such items. The cost of repairing such items shall be charged to the appropriate account in operating expenses.

(3) Scrap and nonusable material included in this account shall be carried at the estimated amount which will be received therefor. The difference between the amounts realized for scrap and nonusable material sold and the amounts at which it is carried in this account, so far as practicable shall be adjusted in the accounts credited when the material was taken up in this account.

NOTE A.—Interest paid on material bills the payments of which are delayed shall be charged to account 336.

NOTE B.—Inventories of material and supplies shall be taken during each calendar year and the necessary adjustment to bring this account into harmony with the actual inventory shall be made. In effecting this adjustment, differences which may practicably be assigned to important classes of material shall be equitably adjusted among the accounts to which the classes of material are ordinarily chargeable. Other differences shall be equitably apportioned among the primary accounts to which material has been charged since the last inventory or included in account 704. The company is permitted to equalize over the period between inventories, through debits or credits to account 704 and concurrent credits or debits to account 122, the estimated amount, based on the company's past experience, of the overage or shortage which will occur at the subsequent inventory. Determined differences between the amount of the provision thus made and the actual inventory overage or shortage shall be cleared as provided for in the second and third sentences of this note.

NOTE C.—If, for convenience in accounting and economy in handling material and supplies for nontelephone operations, their cost is included in this account, the company's records shall be so maintained that the cost of such material and supplies so carried can be determined.

123. **Other current assets.**—This account shall include the amount of all current assets which are not includable in accounts 113 to 122, inclusive, such as unmatured rents receivable. (See also instruction 11.)

III. DEFERRED DEBITS

129. **Prepaid rents.**—This account shall include the amounts of rents paid in advance, except minor amounts which may be charged direct to the final accounts. As the term expires for which the rents are paid, this account shall be credited at monthly intervals and the appropriate account charged. (See also instructions 22–B–9, 23–A and accounts 303, 315, 671 and the clearing accounts.)

130. **Prepaid taxes.**—This account shall include the amounts of taxes paid in advance, except minor amounts which may be charged direct to the final accounts. As the term expires for which the taxes are paid, this account shall be credited at monthly intervals and the appropriate account charged. (See also instruction 22–B–8 and accounts 305 and 322.)

131. **Prepaid insurance.**—This account shall include the amount of insurance premiums paid in advance, except premiums chargeable to the telephone plant accounts and minor amounts which may be charged direct to the final accounts. As the term expires for which the premiums are paid, this account shall be credited at monthly intervals and the appropriate account charged.

132. **Prepaid directory expenses.**—This account shall include the cost of preparing, printing, binding, and delivering directories and the cost of soliciting advertisements for directories, except

minor amounts which may be charged direct to account 649, "Directory expenses." Amounts carried in this account shall be cleared to account 649 by monthly charges of such amounts as represent the portion of the expense that is applicable to the respective months. (See also account 649.)

133. **Other prepayments.**—This account shall include prepayments other than those includable in accounts 129 to 132, inclusive, except minor amounts which may be charged direct to the final accounts. As the term expires for which the payments apply, this account shall be credited and the appropriate account charged.

134. **Discount on capital stock.**—This account shall include the net balance, if a debit, in the discount and premium accounts for all classes of capital stock. (See also instruction 14–G.)

135. **Discount on funded debt.**—This account shall include the net balance, if a debit, in the discount, premium and debt expense accounts for all classes of funded debt. (See also instruction 15–G.)

136. **Provident funds.**—This account shall include the amount of cash, the book cost of securities of other companies, and of nominally issued and nominally outstanding (note instruction 3–Q–R) securities issued or assumed by the company, and other assets held by trustees or managers of employees' pension funds, savings funds, relief, hospital, and other association funds (whether contributed by the company, by employees, or by others), when such trustees or managers are acting for the company in the administration of such funds. (See also instructions 12, 13, and 31.)

NOTE.—This account shall not include funds held by trustees when such funds are irrevocably devoted to pension purposes.

137. **Insurance and other funds.**—This account shall include the amount of cash, the book cost of securities of other companies, and of nominally issued and nominally outstanding (note instruction 3–Q–R) securities issued or assumed by the company and other assets held by trustees or managers (including workmen's compensation commissions) of insurance and other funds which have been specifically set aside or invested for specific purposes not provided for elsewhere. A separate account shall be kept for each fund under titles which will designate the obligation in support of which the fund is created. (See also instructions 12, 13, and 31.)

138. **Extraordinary maintenance suspense.**—(A) This account shall include the unprovided-for loss in service value of telephone plant retired in accordance with provisions of instruction 83. (See also account 609.)

(B) This account shall include also the cost of extensive replacements of station apparatus, inside, drop and block wires, in accordance with the provisions of instruction 64. (See also account 605.)

(C) Charges provided in paragraphs (A) and (B) shall be included in this account only after permission of this Commission has been obtained. The company's application to this Commission

for such permission shall give full particulars concerning the property retired or of the extensive replacements of apparatus or wires, the amount chargeable to operating expenses, and the period over which in its judgment, the amount of such charges should be distributed.

139. **Other deferred debits.**—This account shall include all deferred debits, other than those provided for in accounts 129 to 138, inclusive, such as unaudited amounts and other debit balances in suspense that can not be cleared and disposed of until additional information is received; debit balances in clearing accounts; the amount, pending determination of loss, of funds on deposit with banks which have failed; assets of current character but of doubtful value (see also instruction 11); revenue, expense, and income items held in suspense (see also instruction 6); amounts paid for options pending final disposition; the cost of preliminary surveys, plans, investigations, etc., made for determining the feasibility of projects under contemplation. This account shall include also the cost of valuations, inventories, and appraisals taken in connection with the contemplated purchase or sale of property. If the property is subsequently purchased, the preliminary costs shall be charged to the appropriate telephone plant or other accounts, or if it is sold, such costs shall be deducted from the sale price in accounting for the property sold; if other contemplated projects are carried out, the preliminary costs shall be included in the cost of the projects; if the contemplated projects are abandoned, such costs (including options paid, if any) shall be charged to account 413, "Miscellaneous debits to surplus."

IV. Stock

150. **Capital stock.**—(A) This account shall include the book liability for certificates which represent permanent interests in the company or interests which if terminable are so only at the option of the company, as follows:

(1) For actually outstanding stock. (Note instruction 3–C).

(*a*) The par value of par stock.

(*b*) The current money value at time of sale of the consideration received for nonpar stock. (See also notes A and B to this account.)

(*c*) Appropriations of surplus which have been transferred to nonpar stock account.

(2) For nominally issued and nominally outstanding stocks. (Note instructions 3–Q–R and 13–B.)

(*a*) The par value of par stock.

(*b*) Any nominal value assigned to nonpar stock.

(B) This account shall be kept so as to show the book liability for stocks included herein classified according to preferences in distribution of dividends or assets, difference in voting rights, and difference in conditions under which they may be retired.

(C) To this account shall be charged at the time of retirement the book liability for all stock retired.

NOTE A.—When a general levy or assessment is made against holders of par stock requiring the payment of any sum in addition to the consideration agreed upon at the time of the sale, the amount collected upon such levy or assessment shall be credited to the discount and premium account for the class of stock on which the assessment is made. If such levy or assessment is made against the holders of nonpar stock, the amount collected shall be added to the book liability carried in this account for such stock.

NOTE B.—No debits shall be made to this account for nonpar stock except for the reacquirement of the stock or for amounts distributed to stockholders in liquidation.

NOTE C.—No entries shall be made in this account for stock certificates before the certificates have been lawfully authorized and authenticated.

151. **Stock liability for conversion.**—This account shall include the company's liability under agreements to exchange its capital stock for the outstanding securities of other companies which have not been surrendered for exchange.

NOTE.—When prior to their actual conversion the securities outstanding have been given all rights and privileges of capital stock of the company's own issue, such securities shall be included in account 150.

152. **Premium on capital stock.**—This account shall include the net balance, if a credit, in the discount and premium accounts for all classes of capital stock. (See also instruction 14–G.)

153. **Capital stock installments.**—(A) This account shall include amounts received on account of subscriptions to capital stock prior to the issuance of the stock.

(B) As the total amount of each subscription is received and stock certificates are issued this account shall be cleared; the book liability for the certificates shall be included in account 150, "Capital stock," and any discount or premium involved shall be included in the appropriate discount and premium account.

(C) There shall be shown under this account in the short column of the balance sheet, the total amount of the capital stock subscriptions which have not been fully paid or canceled and also the total amount unpaid on such subscriptions.

V. LONG-TERM DEBT

154. **Funded debt.**—(A) This account shall include the total face value of unmatured debt, maturing more than one year from date of issue, issued by the company and not retired and the total face value of similar unmatured debt of other companies, the payment of which has been assumed by the company, including funded debt the maturity of which has been extended by specific agreement. (See also instructions 13 and 15.)

(B) This account shall be kept so as to show the face value of: (1) Nominally issued funded debt, (2) actually outstanding funded debt, and (3) nominally outstanding funded debt. (Note instructions 3–C–Q–R.)

(C) The amounts included herein shall be further divided so as to show the amount of each class of funded debt as follows:

(1) *Mortgage bonds.*—Bonds secured by lien on physical property and not includable in the other subdivisions of this account.

(2) *Collateral trust bonds.*—Bonds and notes secured by a lien on securities or other negotiable paper, and stock trust certificates that are similar in character to collateral trust bonds.

(3) *Income bonds.*—Bonds which are a lien on a company's revenue alone, or bonds which, while being a lien on its property and franchises, can claim payment of interest only in case interest is earned.

(4) *Miscellaneous obligations.*—All funded obligations not provided for by the other subdivisions of this account, including unsecured certificates of indebtedness, debenture bonds, plain bonds, and other similar obligations maturing more than one year after date of issue.

(5) *Receipts outstanding for funded debt.*—Amounts received on account of subscriptions to funded debt, except that amounts received in excess of the total face value of any issue of funded debt under subscription shall be accounted for as a premium and included in the appropriate discount, premium, and debt expense account. (See also instruction 15.) As the total amount of each subscription is received and evidences of indebtedness are issued, this subaccount shall be cleared; the face value of the funded debt shall be included in the proper subdivision of this account and any discount or premium involved shall be included in the appropriate discount and premium account.

(D) Each of the above classes shall also be divided into subclasses according to differences in mortgage or other lien or security therefor, rate of interest, interest dates, or date of maturity.

NOTE A.—Securities maturing one year or less from date of issue shall be included in account 153, except that where an issue of securities maturing serially over a period of more than one year contains short-term obligations, such obligations shall be included as funded debt.

NOTE B.—Matured funded debt shall be included in account 163.

NOTE C.—Investment advances, including those represented by notes (note instruction 3–M), shall be included in account 156 or account 157, as may be appropriate.

155. **Receivers' certificates.**—When any receiver acting under the orders of a court is in possession of the property of the company and under the orders of such court issues evidences of indebtedness chargeable upon such property, the face value of such evidences of indebtedness shall be credited to this account.

156. **Advances from affiliated companies.**—This account shall include the amount of investment advances (note instruction 3–M) from affiliated companies (note instruction 3–D).

NOTE.—Amounts due affiliated companies which are subject to current settlement shall be included in account 159 or other appropriate account.

157. **Other long-term debt.**—This account shall include investment advances (note instruction 3–M) from nonaffiliated companies (note instruction 3–S) or individuals, and other long-term debt not provided for elsewhere.

NOTE.—Amounts due nonaffiliated companies or individuals which are subject to current settlement shall be included in account 159 or other appropriate account.

VI. Current Liabilities

158. **Notes payable.**—This account shall include the face value of notes, drafts, and other evidences of indebtedness issued or assumed by the company (except interest coupons) which are payable on demand or not more than one year from date of issue.

Note A.—Obligations which mature more than one year after the date of issue, obligations maturing serially any part of which matures more than one year after date of issue, and notes representing investment advances (note instruction 3-M) shall be included in accounts 154, 156, or 157, as appropriate.

Note B.—All unmatured receivers' certificates, regardless of date of maturity, shall be included in account 155.

159. **Accounts payable.**—(A) This account shall include amounts currently due to others and not provided for in other accounts, such as those for wages, traffic settlements, material and supplies, repairs to telephone plant, matured rents, and interest payable under monthly settlements on short-term loans, advances, and open accounts.

(B) In the balance sheet statement there may be included in this account the net amount payable to companies in favor of each of which there is a net credit balance between this account and account 120, "Accounts receivable."

160. **Customers' deposits.**—This account shall include the amount of cash deposited with the company by customers as security for the payment for telephone service.

Note.—Advance payments made by prospective customers prior to the establishment of service shall be credited to account 161.

162. **Matured interest and dividends.**—This account shall include the amount of matured and unpaid interest on indebtedness of the company, and receivers' certificates, and the amount of dividends due and payable on capital stock but unpaid, uncalled for, or unclaimed at the date of the balance sheet.

Note.—Interest payable under monthly settlements on short-term loans, advances, and open accounts shall be included in account 159.

163. **Matured funded debt.**—This account shall include the amount (including any obligations for premiums) of funded debt and receivers' certificates matured and unpaid without any specific agreement for extension of maturity, including unpresented bonds drawn for redemption through the operation of sinking and redemption fund agreements.

164. **Advance billing and payments.**—This account shall include the amount of advance billing creditable to revenue accounts in future months; also advance payments made by prospective customers prior to the establishment of service. Amounts included in this account shall be credited to the appropriate revenue accounts in the months in which the service is rendered, or cleared from this account as refunds are made.

165. **Other current liabilities.**—This account shall include all liabilities of a current character which are not includable in accounts 158 to 164, inclusive.

VII. Accrued Liabilities Not Due

166. **Taxes accrued.**—This account shall include the amount of unpaid taxes accrued. (See also instruction 22–B–8 and accounts 305 and 322.)

Note.—Taxes paid in advance shall be included in account 130.

167. **Unmatured interest, dividends, and rents accrued.**—(A) This account shall include the amount of interest on indebtedness of the company and receivers' certificates, dividends on capital stock, and rents accrued to the date for which the balance sheet is made, but not payable until after that date.

(B) This account shall be so maintained as to show separately the amount of interest, of dividends, and of rents accrued to the date of the balance sheet.

Note A.—Matured rents are includable in account 159, and matured dividends and interest in account 162.

Note B.—Interest payable under monthly settlements on short-term loans, advances, and open accounts shall be included in account 159.

VIII. Deferred Credits and Reserves

168. **Premium on funded debt.**—This account shall include the net balance, if a credit, in the discount, premium, and debt-expense, accounts for all classes of funded debt. (See also instruction 15–G.)

169. **Insurance reserve.**—(A) To this account shall be credited appropriations of income or surplus specifically made to cover self-carried risks for losses through accident, fire, flood, or other cause.

(B) In case the company elects to carry its own risks for losses through accident, fire, flood, or other cause and provides a reserve, other than provision made in the depreciation reserve, to equalize anticipated losses, the charges to account 668, "Insurance," and other appropriate accounts to cover such risks shall be credited to this account. Such charges and credits shall be upon the basis of rates which fairly cover the risks insured. These rates should be determined according to the company's experience and best estimate as to the hazard covered. A schedule of risks covered by this reserve shall be maintained giving a description of the property or the character of the risks covered.

(C) If the company reinsures with insurance companies risks initially covered in this account, the premiums for such reinsurance shall be charged hereto and the amounts recovered under such commercial insurance shall be credited hereto.

(D) To the extent that losses and damages sustained are covered by this account, an amount equal thereto shall be charged to this account and credited to the accounts appropriate for the losses and damages sustained.

Note.—All losses and damages sustained, including those covered by commercial insurance or by this account, shall be charged in the first instance to the depreciation reserve, telephone plant, repair, accidents and damages, or other appropriate account according to the character of the loss. Insurance recoverable or chargeable to this account on account of losses and damages sustained shall be credited to the account to which the losses and damages are chargeable.

170. **Provident reserve.**—(A) This account shall include specific appropriations of income or surplus and the amounts contributed by employees or others (whether carried in special trust funds or in the general funds of the company) for pensions, accident and death benefits, savings, relief, hospital and other provident purposes, when administered by trustees or managers acting for the company.

(B) This account shall include also the amount accrued for pensions through charges to account 672, "Relief and pensions." Amounts so credited shall, when actually paid to retired employees or paid into a trust fund irrevocably devoted to the payment of pensions, be charged hereto.

171. **Depreciation reserve.**—(A) This account shall be credited with amounts concurrently charged to account 608, "Depreciation," and account 702, "Vehicle and other work equipment expense," for currently accruing depreciation (note instruction 3–J) of telephone plant (see also instructions 80, 81, and 82). It shall also be credited with any amounts which the company may elect to charge to account 413, "Miscellaneous debits to surplus," and transfer to this account in respect of past accrued depreciation not provided for. (See also instructions 20–C and 21.)

(B) At the time of retirement of depreciable telephone plant, this account shall be charged with the book cost of the property retired plus the cost of removal (except the cost of removal of station apparatus) and shall be credited with the salvage value and insurance recovered, if any. It shall be credited with amounts chargeable to account 138, "Extraordinary maintenance suspense," as provided in instruction 83. (See also instruction 25.)

(C) For corporate ledger and balance sheet purposes this account shall be regarded and treated as a single composite reserve. However, for purposes of analysis, each company shall maintain subsidiary records in which the depreciation reserve is broken down into component parts corresponding to the primary telephone plant accounts which include depreciable telephone plant (see also instruction 82); these subsidiary records shall show the current credits and debits to the reserve in complete detail by such primary plant accounts.

172. **Amortization reserve.**—(A) This account shall be credited with amounts concurrently charged to account 671, "Operating rents," account 673, "Telephone franchise requirements," and account 675, "Other expenses," for the amortization of leaseholds, franchises, and patents, respectively. (See also instruction 25–E.)

(B) This account shall also be credited with any amounts concurrently charged to account 413, "Miscellaneous debits to surplus," to provide a reserve for the retirement of amounts carried in account 201, "Organization," and account 278, "Undistributed cost of property." (See also note to this account.)

(C) When any leasehold carrier in account 211, "Land," or any franchise or patent expires, is relinquished or otherwise retired from

service, this account shall be charged with the amount previously credited hereto in respect of the property going out of service. The book cost of the property so retired less the amount chargeable to this account and less the proceeds realized at retirement shall be included in the appropriate surplus account. (See accounts 315 and 174 for depreciation on miscellaneous physical property.)

(D) When amounts carried in account 201, "Organization," or account 278, "Undistributed cost of property," are retired, this account shall be charged with any amount previously credited hereto in respect of the property retired.

NOTE.—It is not required that a reserve be maintained for the retirement of amounts carried in accounts 201 and 278.

173. **Employment stabilization reserve.**—(A) This account shall be credited with amounts concurrently charged to account 611, "Employment stabilization." When maintenance work for which provision has been made in this account is performed, this account shall be charged with an amount equal to the cost of such work and concurrently account 611 shall be credited.

(B) This account shall also be credited with amounts concurrently charged to account 672, "Relief and pensions," under provisions of paragraph (F) of that account to provide a reserve for termination allowances or similar benefits to employees of the company when such employees are laid off because of lack of work, also to provide necessary and warranted relief to former employees. When disbursements are made for these purposes they shall be charged to this account.

174. **Other deferred credits.**—(A) This account shall include the amount of all deferred credits not includable in accounts 168 to 173, inclusive, such as credit balances in clearing accounts; estimated uninsured casualty liabilities charged to account 669, "Accidents and damages"; amounts awaiting adjustments between accounts; amounts accrued for depreciation of miscellaneous physical property; and revenue, expense, and income items in suspense. (See also instruction 6.)

(B) When miscellaneous physical property not previously used in telephone service is disposed of, this account shall be charged with the amount previously credited hereto in respect of such property and the book cost of the property so retired less the amount chargeable to this account and less the value of the salvage recovered or the proceeds from the sale of the property shall be included in the appropriate surplus account. In case the property had been used in telephone service previous to its inclusion in account 103, "Miscellaneous physical property," the amount accrued for depreciation thereon after its retirement from telephone service shall be charged to this account and credited to account 171, "Depreciation reserve," and the accounting for its retirement from account 103 shall be in accordance with that applicable to telephone plant retired. (See also instruction 25.)

IX. Donations for Telephone Plant

175. **Donations.**—This account, in accordance with instruction 20–C, shall include the amounts of money or its equivalent donated for the construction or acquisition of telephone property. The amount of such donation shall be permanently carried in this account.

X. Surplus

180. **Surplus reserved.**—This account shall include all amounts, not provided for elsewhere, reserved from surplus including those reserved by charges to income and surplus, such as appropriations of income or surplus to sinking and other fund reserves and reservations charged to income or surplus in respect of operating revenues subject to possible refund under rate litigations.

181. **Unappropriated surplus.**—(A) An account under this title shall be maintained in the general books of the company. The balance of all surplus primary accounts (400 to 416, inclusive) shall be closed into this account at the end of each calendar year. (See also instruction 40.)

(B) If the balance in this account is a deficit, it shall be shown in red in the balance sheet of the report to this Commission.

TELEPHONE PLANT ACCOUNTS

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PLANT ACCOUNTS

(Note particularly instructions 20 to 25, inclusive)

201. **Organization.**—This account shall include the cost of organizing and incorporating the company, and the expense of issuing capital stock. (See also instructions 14 and 15.)

ITEMS

[Note instruction 8]

Amounts paid for legal services.
Amounts paid for privileges of incorporation.
Fees and commissions paid, including cash value of securities issued, to promoters, underwriters, brokers, and salesmen.
Fees and taxes for issuance of capital stock.
Listing capital stock on exchanges.
Office expenses incident to organizing and preparing the company for operation.
Preparing, engraving, printing, issuing, and distributing prospectuses and certificates in connection with original and additional stock issues.
Revenue stamps on new issues of capital stock.
Soliciting subscriptions for stock, including fees, commissions, and advertising.
Special counsel and other fees and expenses in mergers, consolidations, and reorganizations.

NOTE A.—Whenever all or any portion of an issue of capital stock is retired, the proportionate part of the amounts included in this account for expenses incurred in connection with such issue shall be retired.

NOTE B.—When charges are made to this account for expenses incurred in mergers, consolidations, or reorganizations, amounts previously included herein on the books of the various companies concerned should not be carried over unless it is clear that such items involve no duplication when added to the new charges made or to be made.

202. **Franchises.**—This account shall include the cost of governmental franchises and similar rights running for more than one year which are necessary in the conduct of the company's telephone operations. It shall include amounts paid in cash and the cost of plant, material, supplies, and equipment given as the initial consideration for such franchises; cost of advertising, governmental election costs assumed by the company, and similar expenses incurred in procuring such franchises; also the original cost of franchises acquired by assignment. This account shall include amounts, other than those includable in account 201, "Organization," paid to municipalities or other governmental agencies as a condition precedent to engaging in business, whether or not the right to occupy city property, streets, and highways is obtained in connection therewith. (See also instruction 22–B–7.)

NOTE A.—The cost of franchises running for one year or less after acquisition shall be charged to account 673, or, if such franchises extend beyond the current year, to account 133. Franchises acquired at small cost may be charged to account 673 irrespective of their term of life.

NOTE B.—Franchise taxes (payable annually or more frequently) shall be charged to account 365.

NOTE C.—This account shall not include the cost of plant, material and supplies, or equipment furnished to municipalities or other governmental authorities when given other than as initial consideration for franchises or similar rights. (See also account 673.)

203. **Patent rights.**—This account shall include the cost of patent rights having a life of more than one year from date of acquisition for use in connection with the company's telephone operations.

NOTE.—The cost of patents having a life of one year or less, patents acquired at small cost or in an undeveloped state, patents of doubtful service value, and similar expenditures on account of patents shall be charged to account 675.

207. **Right of way.**—This account shall include the cost of land, and of leaseholds, easements, and similar rights in land having a term of more than one year, acquired for the location of pole line, cable, wire, and conduit plant, also the cost of permits to erect poles and to place conduit when the expected period of occupancy under such permits exceeds the estimated life of the initial plant installed. It shall include the related portion of the pay and expenses of right-of-way agents and other costs of acquiring such land, rights, and permits.

NOTE A.—The cost of permits to erect poles and to place conduit when the expected period of occupancy under such permits does not exceed the estimated life of the initial plant installed, also the cost of other permits not includable in this account, such as those to place cable and wire on buildings and fences, and the related pay and expenses of employees and other costs incident to acquiring such permits shall be included in the account appropriate for the cost of the property constructed. (See also instruction 22–B–7.)

NOTE B.—Annual or more frequent payments for the use of right of way shall be charged to account 671.

NOTE C.—Payments to municipalities or other governmental agencies (exclusive of franchise taxes) as consideration for a franchise or right to conduct the company's tele-

phone operations, whether or not the right to occupy city property, streets, and highways is obtained thereunder, shall be accounted for as franchise payments. (See also accounts 202 and 673.)

211. **Land.**—(A) This account shall include the cost of land and of leaseholds, easements, and similar rights in land having a term of more than one year held for general and central office buildings, garages, shops, and for storage and other telephone purposes other than right of way, including the cost of land for which there is a definite plan for its use in telephone service but only after the completion of telephone facilities thereon. It shall include special assessments upon lands for the construction of public improvements. (See also instruction 25–C.)

(B) When land, together with buildings thereon, is acquired the cost shall be fairly apportioned between the land and the buildings and accounted for accordingly. If the plan of acquisition contemplates the removal of the buildings, the total cost of the land and buildings shall be accounted for as the cost of the land, and the salvage value of the buildings when disposed of shall be deducted from the cost of the land so determined. (See also note E to this account.)

ITEMS

[Note instruction 8]

Assessments for the construction of public improvements. (See also note D to this account.)
Clearing or defending title against claims relating to period prior to purchase.
Commissions and fees to brokers, agents, and others.
Condemnation proceedings, including court costs and special counsel fees.
Conveyancer and notarial fees.
Examination and registration of titles.
Grading of land not in connection with buildings.
Relocating property of others in acquisition of land.
Sidewalks on public streets abutting company's property.
Taxes assumed, accrued prior to date of acquisition.
Taxes on land during the period of construction. (See also instruction 22–B–8.)
Voiding leases to secure possession of land acquired.

NOTE A.—Annual or more frequent payments for the use of land shall be charged to the account appropriate for rents.

NOTE B.—When land is acquired for which there is not a definite plan for its use in telephone service, its cost shall be charged to account 103.

NOTE C.—When land is acquired in excess of that required for telephone purposes, the cost of such excess land shall be included in account 103.

NOTE D.—Installments of assessments for public improvements, including interest, if any, which are deferred without option to the company shall be included in this account *only* as they become due and payable. Interest on assessments which are not paid when due shall be included in account 336.

NOTE E.—In case land is purchased for immediate use in a construction project, its cost shall be included in account 280, until such time as the project involved is completed ready for service.

212. **Buildings.**—(A) This account shall include the cost of buildings, and the cost of all permanent fixtures, machinery, appurtenances, and appliances installed as a part thereof. It shall include costs incident to the construction or purchase of a building and to securing possession and title.

(B) When land together with the buildings thereon is acquired and there is a definite plan for their use in telephone service, the purchase price shall be fairly apportioned between the land and buildings, and the amount applicable to the buildings shall be included in this account; the amount applicable to the land shall be included in account 211. (See also account 211.)

ITEMS

[Note instruction 8]

Awnings.
Boilers, furnaces, fixtures, and machinery for heating, lighting, ventilating, and plumbing.
Cable vaults and conduits constructed as part of the building.
Commissions and fees to brokers, agents, architects, and others.
Door checks and door stops.
Drainage and sewerage systems.
Electric wiring.
Elevators.
Fences and hedges.
Fire-extinguisher systems.
Garages, shops, and stables.
General and central office buildings.
Grading, excavating, and preparing grounds for buildings, including laying out of grounds after construction.
Improvements to leased buildings. (See also instruction 23.)
Linoleum and similar floor covering, excluding carpets and rugs.
Motors and generators.
Partitions, including movable.
Piers and foundations for machinery constructed as a permanent part of a building.
Platforms, storage or loading.
Power boards.
Refrigeration systems.
Retaining walls.
Screens, door and window.
Sheds.
Sidewalks, pavements, and driveways on building grounds.
Sprinkling systems.
Storm doors and windows.
Voiding leases to secure possession of buildings acquired.
Water, steam, and gas pipes.
Water-supply systems.
Window shades and ventilators.

NOTE A.—This account shall not include the cost of any telephone equipment or wiring or apparatus for generating or controlling electricity for operation of the telephone system.

NOTE B.—The cost of submarine cable terminal huts shall be included in account 242.

221. **Central office equipment.**—(A) This account shall include the cost of electrical instruments, apparatus, and equipment, other than station equipment, in central offices (including terminal and test rooms), repeater stations and test stations, used in transmitting traffic and operating signals, and similar equipment in operators' schools and other centralized locations.

(B) This account shall also include the cost of operators' chairs, wire chiefs' tools, desks and tables equipped with central office telephone equipment, and other furniture, fixtures, and equipment designed specifically for use in central offices, repeater stations,

etc., or installed as a part of the electrical equipment therein. (See also note A to this account.)

ITEMS

[Note instruction 8]

Aisle-lighting equipment.
Balconies for distributing frames.
Banks-connector, selector.
Batteries.
Battery cabinets.
Boards-floor alarm, power, test, service observing.
Building alterations, minor, such as opening and closing holes in ceilings, partitions, walls, and floors to permit installations of equipment, power conduit, and wiring.
Cables. (See also note B to this account.)
Calculagraphs.
Call registers.
Carrier-current equipment.
Carrier line filters.
Circuit breakers.
Covers for transmission power apparatus.
Desks and tables when equipped with central office telephone equipment. (See also note A to this account.)
Engines, including special foundations not a part of buildings.
Frames-alarm, connector, decoder, decoder connector, line finder, line switch, repeater, selector, sender, test.
Fuse boards.
Fuse panels.
Generators, including special foundations not a part of buildings.
Jumper wires.
Key indicator equipment.
Line filters.
Loading coils. (See also note C to this account.)
Loudspeaker equipment.
Main and intermediate frames.
Meters.
Motors, including special foundations not a part of buildings.
Multiplex apparatus.
Operators' breast plate transmitters.
Operators' chairs.
Operators' head sets.
Platforms, not part of buildings.
Pole changers.
Power circuits for emergency use including payment for installation by others of circuits not owned.
Power plants.
Power panels.
Protectors.
Pulse machines and tone machines.
Radio transmitting and receiving equipment.
Rectifiers.
Relay racks and coil racks
Relays.
Register cabinets.
Repeater sets.
Rheostats.
Ringing machines, including special foundations not a part of buildings.
Rolling ladders.
Switchboards and other electrical equipment used in operators' schools.

Switchboards—subscribers "A" and "B" trunk, toll, dial system.
Switches—connector, line repeater, selector, repeater, test, distributor.
Tarpaulins.
Telegraph instruments and equipment.
Telephotographic equipment.
Teletypewriter switchboards and equipment.
Test boards.
Testing and routining central office equipment prior to assignment to service.
Test tables.
Testing equipment and tools, central office. (See also note D to this account.)
Ticket holders.
Toll ticket carriers.
Turrets.
Water stills for battery service.

NOTE A.—The cost of desks and tables not equipped with central-office equipment, and of kitchen and dining-room equipment, chairs of the same types as used in other offices, typewriters, portable electric fans, etc., shall be charged to account 261.

NOTE B.—The cost of cables leading from the main frame to outside plant shall be charged to account 242.

NOTE C.—The cost of loading coils on circuits leading from the main frame to outside plant shall be included in the account charged with the cost of the circuit of which they are a part.

NOTE D.—The cost of portable testing equipment and tools other than those regularly used in central offices shall be charged to account 264.

231. **Station apparatus.**—This account shall include the cost of station apparatus, installed either for customers' or the company's use, excluding the cost of installation and inside wires.

ITEMS
[Note instructions 8]

Backboards.
Batteries, station.
Battery boxes.
Bell boxes.
Coin collectors.
Cords.
Desk sets, hand sets, and wall sets, including those used at main, extension, private-branch-exchange, and private-line stations, etc. This includes such sets used as operators' sets at private branch exchanges, order turrets and order tables, and those used in central offices and operators' schools. (See also note A to this account.)
Dials.
Extension bells.
Hand set mountings.
Induction coils.
Messenger, and similar signalling devices.
Printer-telegraph equipment.
Program-supply equipment.
Public-address equipment.
Receivers.
Signal cases.
Station switching and signalling devices, including apparatus cabinets, keys, key cabinets, and devices used with intercommunicating systems.
Telegraph equipment.
Teletypewriter equipment.
Transmitters.

NOTE A.—Operators' head sets and breastplate transmitters in central offices and at private branch exchanges and test sets such as those used by wire chiefs, linemen, and others, shall be included in accounts 221, 234, and 264, as appropriate.

NOTE B.—The cost of station protectors is includable in account 232.

232. **Station installations.**—(A) This account shall include the cost of installing station apparatus and the cost of inside wires. Inside wires include:

(1) The wires (or small cables) from the station apparatus to the point near the entrance to the building where the drop or block wire or cable terminates, or to the junction boxes where the house cable or other cable terminates.

(2) The wires (or small cables) used to connect station apparatus in the same building, such as main stations with extension stations, and stations of intercommunicating systems.

(3) The wires (or small cables) used to connect private-branch-exchange switchboards or their distributing frames with terminal stations located in the same building.

(B) This account shall include the cost of clamps, cleats, connecting blocks, ground wires, ground rods, nails, station protectors, screws, and other material used in the installation of station apparatus and inside wires.

NOTE A.—Costs chargeable to this account in connection with cables are restricted to small cables used in station installations instead of wires, such as those run from wall outlets or floor terminals to the station apparatus. The cost of other inside cables, including riser and distributing cables in buildings, which by their physical character, method of installation, and permanence constitute house cables is chargeable to account 242.

NOTE B.—The cost of inside wires (or small cables) installed specifically to serve as trunk, battery, or generator circuits from a private branch exchange to the point of connection with the permanent house or outside cables or wires shall be charged to account 234.

233. **Drop and block wires.**—(A) This account shall include the cost of drop and block wires or service connections, i. e., the portion of a customer's circuit (whether aerial or underground) extending from the inside wire (usually at the station protector or connecting block) or from the station equipment when no inside wire is involved, to the point of connection with the general overhead or underground system. This includes such circuit, carried by means of wire or small cables, extending to the cable terminal in cases where connection is made with a general cable system, or to the point of connection with the aerial wire plant in cases where connection is made with a general wire system. The company shall exercise such precautions as are necessary to prevent credits to this account for aerial wire removed.

(B) This account shall include the cost of brackets, bridle rings, insulators, knobs, span clamps, screws, sleeves, strand, tubes, and other material used in the installation of drop and block wires; the cost of trimming trees and other costs incurred in the installation of such wires; the cost of pipes or other protective covering for underground service connections; and the cost of permits and privileges for construction.

234. **Private branch exchanges.**—This account shall include the cost of private-branch-exchange equipment installed either for customers' or the company's use.

ITEMS

[Note instruction 8]

Attendants' cabinets or cordless switchboards.
Cable or wires from distributing frame to switchboard.
Code call units.
Code sending sets.
Dial system branch exchanges.
Distributing frames.
Inside wires (or small cables used instead of wires) installed specifically to serve as trunk, generator, or battery circuits from a private branch exchange to the point of connection with the permanent house or outside cables or wires.
Operators' chairs.
Operators' head sets and breastplate transmitters.
Order receiving tables.
Order turrets.
Power equipment, including special foundations.
Protectors.
Switchboards.

NOTE A.—The cost of riser and distributing cables in buildings other than central offices, which by their physical characteristics, method of installation, and permanence constitute regular house cable shall be charged to account 242.

NOTE B.—The cost of poles, wires, and cables, whether or not on private property, used to connect the private branch exchange with its terminal stations shall be charged to the pole, wire, and cable accounts.

NOTE C.—The cost of cross connection boxes installed as a part of the house cable system, including those used as the distributing frames for private branch exchanges, shall be charged to account 242.

235. **Booths and special fittings.**—This account shall include the cost of telephone booths and special fittings (exclusive of station apparatus) such as attendants' desks (including equipment or switchboards) counters, railings, chairs, fans, cash registers, directory tables, stands or shelve , and public telephone sign .

241. **Pole lines.**—This account shall include the cost o poles, cross arms, guys, and other material used in the construction of pole lines.

ITEMS

[Note instruction 8]

Anchors.
A and H fixtures.
Bolts.
Braces, pole and back.
Bridge fixtures.
Cable arms.
Clearing routes and tree trimming except maintenance of previous clearings. (See also account 602.)
Crossarms.
Extension arms.
Guard arms.
Guy clamps.
Guy stubs.
Guy wire or strand.
Painting, treating, gaining, roofing, shaving, and stenciling poles.
Permits and privileges for construction. (See also account 207 and instruction 22-B-7.)
Pins.
Pole brackets, wooden.
Poles.

Pole steps.
River crossing and long span fixtures.
Strain insulators.
Towers.

242. **Cable.**—This account shall include the cost of aerial, underground, and submarine cable. It shall include the cost of cable extending from the central office main frame to the point of connection with aerial wire or with drop or block wires or service connections, inside wire or private branch exchange cable, and the cost of interoffice (including intercity) cable; also the cost of cable terminals or boxes, loading coils, and other material used in the construction of the cable plant.

ITEMS

[Note instruction 8]

Bonds and grounds.
Cable—block, feeder, main, subsidiary.
Cable—aerial, buried, submarine, underground.
Cable—house, including riser and distributing cable extending to floor terminal boxes, cross-connection boxes at wall outlets, etc., where connection is made with inside wires.
Cable clamps.
Cable rings.
Cable terminals or boxes.
Cross-connection wires and fuses installed in the first equipment for service of cable terminals or boxes.
Electrolysis surveys made in the course of installing cable.
Floor terminal boxes and cross-connection boxes at wall outlets.
Fuse boxes.
Loading coils, building-out condensers, carrier-line filters and cases therefor.
Main frame terminating cable extending to outside cable.
Negative returns.
Permits and privileges for construction. (See also account 207.)
Pedestals.
Pole seats and balconies.
Pressure contactor-terminals.
Protective covering for buried cable, i. e., cable not run in regular conduit, such as fiber or other material (except when constructed so as to be reusable in place for other cable) and the cost of manholes, etc., designed specifically for use in such construction.
Protectors and arresters.
Pumping out and cleaning manholes and ducts in cable construction work. (See also note A to this account.)
Safety straps.
Sleeves.
Splicing boxes.
Strand, suspension.
Submarine cable terminal huts.
Tree guards.
Trenching for and burying cable not run in regular conduit.
Trolley guards.

NOTE A.—The cost of pumping water out of manholes and of cleaning manholes and ducts in connection with the maintenance or operation of plant shall be charged to account 602.

NOTE B.—The cost of small cables used in station installations instead of wires, such as those run from wall outlets or floor terminals to the station apparatus shall be charged to account 232. The cost of small cables used as drop wires shall be included in account 233.

NOTE C.—The cost of cable leading from central office main frames to other central office equipment shall be charged to account 221.

NOTE D.—The company's records shall be so maintained that the miles of wire in cables may be shown in the annual reports to this Commission.

243. **Aerial Wire.**—This account shall include the cost of aerial wire other than drop and block wires, including insulators, tie wires, and other material used in the construction of aerial wire plant. The company shall exercise such precautions as are necessary to prevent credits to this account for drop and block wires removed.

ITEMS

[Note instruction 8]

Bridle rings.
Bridle wire.
Ground wire, clamps, and rods.
Insulators and thimbles.
Loading coils, building-out condensers, carrier line filters, and cases therefor.
Permits and privileges for construction. (See also account 207.)
Protectors and arresters.
Repeating coils.
Tie wires.
Transposition brackets.
Transposition of circuits in initial construction work and any additions or betterments resulting from transposing or retransposing existing circuits.

NOTE.—The cost of drop and block wires shall be included in account 233.

244. **Underground Conduit.**—This account shall include the cost of tile, pipe, and other conduit, whether underground, in tunnels or on bridges, and of manholes, handholes, and service boxes, including cable racks and other furnishings thereof, and the cost of riser pipe. It shall include the cost of opening trench and repaving in the construction of such plant and the cost of permits and privileges for construction. (See also account 207.)

NOTE A.—The cost of protective covering for buried cable, i. e., cable not run in regular conduit, such as fiber or other material (except when constructed so as to be reusable in place for other cable) and the cost of trenching, manholes, etc., designed specifically for use in such construction shall be charged to account 242.

NOTE B.—The cost of pipes or other protective covering for underground drop and block wires or service connections shall be included in account 233.

261. **Furniture and Office Equipment.**—This account shall include the cost, not provided for in other accounts, of furniture and equipment in offices, storerooms, shops, and other quarters. (See also accounts 221, 234, and 235 and instruction 20–E.)

ITEMS

[Note instruction 8]

Beds, cots, and couches.
Bins, counters, and shelves.
Bookcases.
Cabinets and filing cases.

Cages, cashiers'.
Carpets and rugs.
Chairs.
Clocks.
Davenports.
Desks.
Equipment in rest, dining, recreation, and medical rooms.
Fans, electric, portable.
Fire extinguisher equipment, portable.
Floor scrubbing and polishing machines.
Gas and electric fixtures, portable.
Lockers and wardrobes, portable.
Mirrors, portable.
Motion picture equipment.
Office devices, including addressing, billing, blue printing, computing, dating, duplicating, mailing, photostat and recording machines, cash registers, check writers, postage meter machines, typewriters, etc.
Pianos and phonographs.
Radio sets.
Racks—magazine, newspaper, umbrella, and clothing.
Refrigerators, portable.
Safes.
Sewing machines.
Stoves.
Switchboards, special type public demonstration.
Tables.
Vacuum sweepers.
Vending machines.
Water coolers.

NOTE.—The cost of fixtures attached to and constituting a part of buildings shall be charged to account 212.

264. Vehicles and other work equipment.—This account shall include the cost of vehicles, tools, garage and shop machinery and equipment, and miscellaneous work equipment not provided for in other accounts. (See also instruction 20–8.)

ITEMS

[Note instruction 8]

Air compressors.
Automobiles, motor trucks and tractors, including those equipped with earth-boring machines, pumps, winches, etc.
Blowers, power.
Carts, cable splicer.
Camp wagons, cars, and mounted kitchens.
Compressed air tools.
Concrete mixers and breakers.
Derricks.
Draft animals.
Drills and hammers, power.
Earth-boring machines.
Forges.
Gasoline and oil pumps, portable.
Hand tools.
Hand trucks.
Harness.
Lathes.
Loaders, power.
Motorboats and barges.
Motorcycles and bicycles.

Motors and generators.
Planers.
Pole treating apparatus, chemical.
Pumps.
Tamping and back filling machines.
Tents, cable splicers.
Testing equipment, portable. (See also note B to this account.)
Torches.
Trailers.
Trenching machines.
Wagons.
Winches, power.
Wire measuring machine.

NOTE A.—The cost of chairs, desks, tables, etc., in garages and shops shall be charged to account 261.

NOTE B.—The cost of testing equipment and tools regularly used in central offices shall be charged to account 221.

276. **Telephone plant purchased.**—This account may be charged temporarily with the cost of telephone plant purchased pending distribution to the primary telephone plant accounts. (See also instruction 21.)

NOTE A.—The cost of telephone plant purchased may be distributed to the primary telephone plant accounts upon the basis of estimates subject to appropriate adjustment when final data become available.

NOTE B.—In connection with completing the accounting for telephone plant purchased, appropriate adjustments shall be made in respect of any related depreciation accruals.

277. **Telephone plant sold.**—This account may be credited temporarily with the estimated book cost at the time of retirement of telephone plant sold pending determination of the amounts to be credited to the primary telephone plant accounts. (See also instruction 25–F.)

NOTE A.—Preliminary credits representing the estimated book cost of the telephone plant sold may be made to the primary telephone plant accounts subject to appropriate adjustment when final data become available.

NOTE B.—In connection with completing the accounting for telephone plant sold, appropriate adjustments shall be made in respect of any related depreciation accruals.

278. **Undistributed cost of property.**—This account shall include property costs as carried in account 204, "Other intangible capital," December 31, 1932, and not assignable to other primary accounts provided herein. (See also account 172.) It shall include also amounts as provided in instruction 21–D in respect to telephone plant purchased.

NOTE.—Indirect charges to telephone plant primary accounts such as interest, taxes, insurance, injuries and damages, etc., shall be apportioned to the accounts appropriate for the cost of the physical property involved.

280. **Construction work in progress.**—(A) This account shall include the cost of construction of telephone plant not completed ready for service at the date of the balance sheet including the cost of land acquired for which there is a definite plan for its use in telephone service. It shall include interest during construc-

tion taxes during construction, and all other elements of cost of such construction work. (See also instructions 20 and 22.)

(B) When any telephone plant the cost of which has been included in this account is completed ready for service, the cost thereof shall be credited to this account and charged to the appropriate telephone plant or other accounts.

NOTE A.—It is not required that this account shall include the cost of construction work which will be completed ready for service within a short period, such as the installation of station apparatus, replacements of poles and other work completed within a period of one or two months.

NOTE B.—The balance in this account shall be shown as a separate item under account 100 in the short column of the balance sheet statement in the company's annual report to this Commission.

INCOME STATEMENT

I. Telephone Operating Income

Item

1. Operating revenues (300).
2. Operating expenses (301).
3. Net operating revenues (Item 1 less item 2).
4. Rent from lease of operating property (302).
5. Rent for lease of operating property (303).
6. Operating taxes (305).
7. Net operating income (Items 3 and 4 less items 5 and 6).

II. Other Income

8. Dividend income (312).
9. Interest income (313).
10. Income from sinking and other funds (314).
11. Income from miscellaneous physical property (315).
12. Miscellaneous income (316).
13. Total other income (The sum of items 8 to 12, inclusive).

III. Miscellaneous Deductions from Income

14. Miscellaneous taxes (322).
15. Miscellaneous income charges (323).
16. Total miscellaneous deductions (The sum of items 14 and 15).
17. Income available for fixed charges (Items 7 and 13 less item 16).

IV. Fixed Charges

18. Interest on funded debt (335).
19. Other interest deductions (336).
20. Amortization of discount on funded debt (338).
21. Release of premium on funded debt—Cr. (339).
22. Other fixed charges (340).
23. Total fixed charges (The sum of items 18 to 22 inclusive).
24. Income after fixed charges (Item 17 less item 23).

V. Contingent Interest

25. Contingent interest on funded debt (341).
26. Net income (Net Profit) (Item 24 less item 25).

VI. Disposition of Net Income

27. Contractual reservations of income (342).
28. Miscellaneous reservations of income (343).
29. Dividend appropriations of income (344).
30. Total reservations and appropriations (The sum of items 27 to 29 inclusive).
31. Income balance (400) (Item 26 less item 30).

INCOME ACCOUNTS

(Note particularly instructions 30 and 31)

I. Telephone Operating Income

300. **Operating revenues.**—This account shall include the total revenues for the accounting period which are provided for in the operating revenue accounts 500 to 530, inclusive. (See also instruction 2–C.)

301. **Operating expenses.**—This account shall include the total expenses for the accounting period which are provided for in the operating expense accounts 602 to 677, inclusive. (See also instruction 2–C.)

302. **Rent from lease of operating property.**—(A) This account shall include rents from the exclusive use of telephone operating property held as a whole and operated by others, such as a complete telephone plant, a complete exchange, or a complete toll system.

(B) Rents are creditable to this account whether receivable in cash or disbursed by the lessee in behalf of the company as taxes on the rented property, interest on funded debt, guaranteed dividends on stock or otherwise.

Note.—The rent from property the cost of which is includable in account 103 shall be included in account 315.

303. **Rent for lease of operating property.**—(A) This account shall include rents for the exclusive use of telephone operating property held as a whole and operated by the company, such as a complete telephone plant, a complete exchange, or a complete toll system.

(B) This account shall include also taxes borne by the lessee of property, the rent for which is chargeable to this account.

(C) Rents are chargeable to this account whether payable in cash or disbursed by the lessee in behalf of the lessor as taxes on the rented property, interest on funded debt, guaranteed dividends on stock or otherwise.

Note A.—If leased telephone plant the rent for which is chargeable to this account is sublet to others, the rent receivable therefrom shall be credited to the account appropriate for rent from owned property of the same class.

Note B.—Rents payable for property used by the company for other than telephone operations shall be included in account 315.

Note C.—Charges for depreciation of telephone operating property leased as a whole and operated by the company shall be included in account 608 or account 702, as appropriate, on the same basis as for owned property (see also instruction 31) when the company is responsible for depreciation under the terms of the lease.

305. **Operating taxes.**—(A) This account shall include all Federal, State, County, Municipal, and other taxing-district taxes, including franchise taxes payable annually or more frequently,

relating to telephone property, operations, and privileges for the period for which the income account is stated. Taxes accrued through this account prior to their payment shall be credited to account 166, "Taxes accrued."

(B) Taxes on leased telephone plant shall be included in this account by the owner. Any taxes on rented telephone plant which are borne by the lessee shall be appropriately credited by the owner to account 524, "Rent revenues," or account 302, "Rent from lease of operating property," and charged by the lessee to account 671, "Operating rents," or account 303, "Rent for lease of operating property."

NOTE A.—Taxes on other than telephone property, operations, and privileges shall be charged to account 322.

NOTE B.—Special assessments for street and other improvements and special benefit taxes, such as water taxes and the like, shall be included in the operating expense accounts or investment accounts, as may be appropriate.

NOTE C.—Discount allowed for prompt payment of taxes shall be credited to the account to which the taxes are chargeable.

NOTE D.—Interest on tax assessments which are not paid when due shall be included in account 336.

NOTE E.—The accounting for taxes on physical property during construction and before the facilities are completed ready for service shall be in accordance with instruction 22-B-8.

NOTE F.—Taxes paid by the company under tax-free covenants on indebtedness shall be charged to account 340.

II. OTHER INCOME

312. **Dividend income.**—(A) This account shall include dividends on stock, the income from which is the property of the company, whether such stock is owned by the company and held in its treasury, or deposited in trust (except in sinking or other funds, see note B to this account) or controlled through lease or otherwise.

(B) Dividends shall not be credited to this account before actual collection, unless their payment is reasonably assured by past experience, guaranty, anticipated provisions, or otherwise.

NOTE A.—These accounts (note instruction 3-A) shall not include dividends or other returns on securities issued or assumed by the company and held by or for it, whether pledged as collateral, or held in its treasury, in special deposits or in sinking or other funds.

NOTE B.—Dividends on stocks of other companies held in sinking or other funds shall be credited to account 314.

313. **Interest income.**—(A) This account shall include interest on securities, including notes and other evidences of indebtedness, the income from which is the property of the company, whether such securities are owned by the company and held in its treasury, or deposited in trust (except in sinking or other funds, see note B to this account) or controlled through lease or otherwise. It shall include also interest on bank balances, certificates of deposits, open accounts, and other analogous items.

(B) Interest shall not be credited before actual collection, unless its payment is reasonably assured by past experience, guaranty, anticipated provisions, or otherwise.

(C) This account shall be credited with such amounts as are charged to the telephone plant accounts for interest on funds expended for construction purposes, as provided in instruction 22–B–10.

(D) There may be included in this account for each month or other accounting period the applicable amount requisite to extinguish, during the interval between the date of acquisition and date of maturity, the difference between the purchase price and the par value of securities owned, the income from which is includable in this account. Amounts thus credited or charged shall be concurrently included in the accounts in which the securities are carried. Any such difference remaining unextinguished at the sale or at the maturity and satisfaction of such securities shall be cleared to account 413, "Miscellaneous debits to surplus," or account 402, "Miscellaneous credits to surplus."

NOTE A.—These accounts (note instruction 3–A) shall not include interest or other returns on securities issued or assumed by the company and held by or for it, whether pledged as collateral, or held in its treasury, in special deposits, or in sinking or other funds.

NOTE B.—Interest on cash and on securities issued by others shall be included in account 314 when such assets are held in sinking or other funds.

NOTE C.—Cash discount on bills for material purchased shall not be included in this account. (See also account 122.)

314. **Income from sinking and other funds.**—(A) This account shall include the income accrued on cash, securities issued by other companies, and other assets (not including securities issued or assumed by the company) held in sinking and other funds.

(B) There may be included in this account for each month or other accounting period the applicable amount requisite to extinguish, during the interval between the date of acquisition and the date of maturity, the difference between the purchase price and the par value of securities held in sinking or other funds. Amounts thus credited or charged shall be concurrently included in the accounts in which the securities are carried. Any such difference remaining unextinguished upon the maturity and satisfaction of such securities shall be cleared to account 413, "Miscellaneous debits to surplus," or account 402, "Miscellaneous credits to surplus."

NOTE.—Income from sinking and other funds required to be held in such funds, and credits to reserve accounts representing income from funds, shall be accounted for as provided in instruction 31.

315. **Income from miscellaneous physical property.**—This account shall include the net balance of the revenues from and the expenses (including depreciation and insurance) of physical property the cost of which is includable in account 103, "Miscellaneous physical property," and also of physical property of others leased and used by the company for other than telephone operations. The rent for leased property which is used by the company for other than telephone operations, assessments when borne by the

company for maintenance of public improvements against property the cost of which is includable in account 103, and directly assignable administration expenses incident to operation of miscellaneous physical property, shall be included in this account.

NOTE A.—Net credit balances shall be shown in the income statement of the report to this Commission in black and net debit balances in red.

NOTE B.—Taxes on miscellaneous physical property shall be included in account 322.

316. **Miscellaneous income.**—This account shall include all items, not provided for elsewhere, properly creditable to Income.

ITEMS TO BE CREDITED

[Note instruction 8]

Fees collected in connection with the exchange of coupon bonds for registered bonds

Profits from the telephone operations of other companies realized by the company under contracts.

Profits realized from custom work performed for others not incident to the company's telephone operations.

III. MISCELLANEOUS DEDUCTIONS FROM INCOME

322. **Miscellaneous taxes.**—This account shall include all taxes not provided for elsewhere, such as taxes on miscellaneous physical property. (See also instruction 22–B–8.) Taxes accrued through this account prior to their payment shall be credited to account 166, "Taxes accrued."

NOTE A.—Special assessments for street and other improvements and special benefit taxes, such as water taxes and the like, shall be included in the operating expense accounts or investment accounts, as may be appropriate.

NOTE B.—Discounts allowed for the prompt payment of taxes shall be credited to the account to which the taxes are chargeable.

NOTE C.—Interest on tax assessments which are not paid when due shall be included in account 336.

323. **Miscellaneous income charges.**—This account shall include all items not provided for elsewhere properly chargeable to Income.

ITEMS TO BE CHARGED

[Note instruction 8]

Current expenses of trustees in maintaining and administering trusts incident to outstanding debt of the company.

Membership fees and dues in associations which do not have some direct or intimate relation to the telephone operations of the company.

Uncollectible amounts previously credited to accounts 312 to 316, inclusive. (See also instruction 11 and note to account 530.)

IV. FIXED CHARGES

335. **Interest on funded debt.**—(A) This account shall include the current accruals of interest on all classes of debt the principal of which is includable in account 154, "Funded debt," and account 155, "Receivers' certificates," except interest provided for in account 341, "Contingent interest on funded debt." (See also instruction 22–B–10.) It shall include the interest on funded

debt the maturity of which has been extended by specific agreement.

(B) This account shall be kept in such form that the interest on each class of funded debt and on receivers' certificates may be shown separately in the annual report to this Commission.

NOTE A.—These accounts (note instruction 8-A) shall not include charges for interest on funded debt issued or assumed by the company and held by or for it, whether pledged as collateral or held in its treasury, in special deposits, or in sinking or other funds.

NOTE B.—Interest expressly provided for and included in the face amount of securities issued shall be charged at the time of issue to account 133 and cleared to this account as the term expires to which the interest applies.

336. Other interest deductions.—(A) This account shall include all interest deductions not provided for elsewhere. Discount, premium, and expense on notes maturing one year or less from date of issue shall be included in this account in equal monthly installments throughout the term of the notes or included herein at the time such notes are issued. (See also instruction 22–B–10.)

(B) A list of representative items of indebtedness follows, the interest on which is chargeable to this account (note instruction 8):

Advances from affiliated companies. (See also account 156.)
Advances from nonaffiliated companies, and other liabilities included in account 157.
Assessments for public improvements past due.
Bond coupons, matured and unpaid.
Capital stock subscriptions, receipts for installments on.
Claims and judgments.
Customers' deposits.
Funded debt matured, with respect to which a definite agreement as to extension has not been made.
Notes payable on demand or maturing one year or less from date of issue.
Open accounts.
Tax assessments, past due.

NOTE.—Interest payable on notes or other evidences of indebtedness maturing serially shall be charged to account 335 if any portion of the obligation matures more than one year from date of issue.

338. Amortization of discount on funded debt.—This account shall include during each month or other accounting period such proportion of the unamortized debit balance in each particular discount, premium, and expense account for actually outstanding funded debt as is applicable to that period. This proportion shall be determined in accordance with instruction 15.

339. Release of premium on funded debt—Cr.—This account shall include during each month or other accounting period such proportion of the unextinguished credit balance in each particular discount, premium, and expense account for actually outstanding funded debt as is applicable to that period. This proportion shall be determined in accordance with instruction 15.

340. Other fixed charges.—This account shall include all items of fixed charges not provided for elsewhere properly chargeable to income of the accounting period, such as taxes paid by the company under tax-free covenants on indebtedness.

V. Contingent Interest

341. Contingent interest on funded debt.—This account shall include accrued interest payable on funded debt, when a claim against income after fixed charges and prior to the interests of stockholders in the earnings of the company, such as interest on income bonds.

VI. Disposition of Net Income

342. Contractual reservations of income.—This account shall include reservations chargeable to income, when specifically required under the terms of mortgages, deeds of trust, orders of courts, contracts, or other agreements. (See also instruction 31.)

Note A.—Reservations of income resting in the discretion of the company (i. e., not required by mortgages, contracts, etc.) shall be charged to account 343.

Note B.—Amounts charged to this account shall be concurrently credited to the appropriate reserve accounts.

343. Miscellaneous reservations of income.—This account shall include reservations of income for purposes not provided for elsewhere and not specifically required under terms of mortgages, contracts, etc. It shall include appropriations for investment in telephone plant, and income reserved at the company's discretion on account of rate litigations, etc. (See also instruction 31.)

Note.—Amounts charged to this account shall be concurrently credited to the appropriate reserve accounts.

344. Dividend appropriations of income.—(A) This account shall include dividends on capital stock actually outstanding, if chargeable to income.

(B) If a dividend is not payable in cash, the consideration shall be described in the entry with sufficient particularity to identify it.

(C) This account shall be kept in such form that the dividends on each class of capital stock may be shown separately in the annual report to this commission.

Note A.—These accounts (note instruction 3-A) shall not include charges for dividends on capital stock issued or assumed by the company and held by or for it, whether pledged as collateral, or held in its treasury, in special deposits or in sinking or other funds.

Note B.—Dividend appropriations of surplus shall be charged to account 416.

SURPLUS STATEMENT

CREDITS:

181. Unappropriated surplus (at beginning of period).[1]
400. Income balance.[2]
401. Credits for telephone plant sold.
402. Miscellaneous credits to surplus.

DEBITS:

410. Debits for telephone plant sold.
413. Miscellaneous debits to surplus.
414. Contractual reservations of surplus.
415. Miscellaneous reservations of surplus.
416. Dividend appropriations of surplus.
181. Unappropriated surplus (at end of period).[1]

SURPLUS ACCOUNTS

(Note particularly instruction 40)

400. **Income balance.**—An account, under this title, shall be maintained in the general books of the company. The balance of all income primary accounts (300 to 344, inclusive) shall be closed into this account at the end of each calendar year.

401. **Credits for telephone plant sold.**—This account shall include amounts creditable to surplus in accordance with instructions 25–C and 25–F, in connection with the sale of telephone plant.

402. **Miscellaneous credits to surplus.**—This account shall include amounts creditable to surplus not provided for elsewhere. Among the items which shall be credited to this account are (note instruction 8):

Amount of the credit balance in discount, premium and expense account relating to funded debt reacquired at the time of its reacquirement. (See also instruction 15–E.)

Amount of the credit balance in the discount and premium account relating to capital stock reacquired at the time of its reacquirement. (See also instruction 14–E.)

Amounts received for abrogation of contracts.

Credits for amounts previously written off through charges to surplus.

Credits resulting from adjustments required to bring to par securities issued or assumed by the company and reacquired at a cost less than the par value. (See also instruction 13.)

Delayed credits to income, operating revenue, and operating expense accounts as provided in instruction 5.

Forfeitures of amounts deposited under options for the sale or lease of property.

Profit derived from the sale of securities of other companies.

Profit derived from the sale of property carried in account 103. (See also account 174.)

Profit derived from the sale of unexpired leases.

Unclaimed customers' deposits.

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[1] If a deficit, the balance shall be shown in red.

[2] If a loss, the balance shall be shown in red.

Unclaimed dividends.
Unclaimed wages and vouchered accounts written off.

NOTE.—An analysis of this account will be required in annual reports of the company to this Commission.

410. **Debits for telephone plant sold.**—This account shall include amounts chargeable to Surplus in accordance with instructions 25–C and 25–F, in connection with the sale of telephone plant.

413. **Miscellaneous debits to surplus.**—This account shall include amounts chargeable to surplus not provided for elsewhere. Among the items which shall be charged to this account are (note instruction 8):

Amortization, at company's option, of balances in accounts 201 and 278.
Amortization unprovided for elsewhere.
Amounts charged to surplus to cover past accrued depreciation not provided for. (See also account 171.)
Amount of the debit balance in discount, premium and expense account relating to funded debt reacquired at the time of its reacquirement. (See also instruction 15–E.)
Amount of the debit balance in the discount and premium account relating to capital stock reacquired at the time of its reacquirement. (See also instruction 14–E.)
Amounts charged to surplus to extinguish all or any part of the debit balance in any particular discount and premium account for capital stock actually outstanding. (See also instruction 14–B.)
Amounts charged to surplus to extinguish all or any part of the debit balance in any particular discount, premium, and expense account for funded debt actually outstanding. (See also instruction 15–B.)
Amounts paid for abrogation of contracts.
Appropriations to nonpar stock liability account.
Contributions for charitable or social or community welfare purposes which do not have a direct or intimate relation to the protection of the property of the company or to the development of its business or the welfare of its employees.
Debits resulting from adjustments required to bring to par securities issued or assumed by the company and reacquired at a cost exceeding the par value. (See also instruction 13.)
Delayed debits to income, operating revenue, and operating expense accounts as provided in instruction 5.
Forfeitures of amounts deposited under options for the purchase or lease of property.
Inventory and appraisal costs taken incident to the purchase, sale, or lease property where the transactions are abandoned.
Losses resulting from the sale, destruction, or retirement of property carried in account 103. (See also account 174.)
Losses resulting from the sale of securities of other companies.
Payments of amounts previously written off through credits to surplus.

NOTE.—An analysis of this account will be required in annual reports of the company to this Commission.

414. **Contractual reservations of surplus.**—This account shall include reservations chargeable to surplus when specifically required under the terms of mortgages, deeds of trust, orders of courts, contracts, or other agreements. (See also instruction 31.)

NOTE A.—Reservations of surplus resting in the discretion of the company (i. e., not required by mortgages, contracts, etc.) shall be charged to account 415.

NOTE B.—Amounts charged to this account shall be concurrently credited to the appropriate reserve accounts.

415. Miscellaneous reservations of surplus.—This account shall include reservations of surplus for purposes not provided for elsewhere and not specifically required under terms of mortgages, contracts, etc. It shall include appropriations for investment in telephone plant and surplus reserved at the company's discretion on account of rate litigations, etc. (See also instruction 31.)

NOTE.—Amounts charged to this account shall be concurrently credited to the appropriate reserve accounts.

416. Dividend appropriations of surplus.—(A) This account shall include dividends on capital stock actually outstanding, if chargeable to surplus.

(B) If a dividend is not payable in cash the consideration shall be described in the entry with sufficient particularity to identify it.

(C) This account shall be kept in such form that the dividends on each class of capital stock may be shown separately in the annual report to this Commission.

NOTE A.—These accounts (note instruction 3–A) shall not include charges for dividends on capital stock issued or assumed by the company and held by or for it, whether pledged as collateral, or held in its treasury, in special deposits, or in sinking or other funds.

NOTE B.—Dividend appropriations of income shall be charged to account 344.

OPERATING REVENUE ACCOUNTS

ACCOUNTS FOR CLASS A COMPANIES	ACCOUNTS FOR CLASS B COMPANIES
I. LOCAL SERVICE REVENUES.	I. LOCAL SERVICE REVENUES.
500. Subscribers' station revenues.	500. Local service revenues.
501. Public telephone revenues.	
503. Service stations.	
504. Local private line services.	
506. Other local service revenues.	
II. TOLL SERVICE REVENUES.	II. TOLL SERVICE REVENUES.
510. Message tolls.	510. Toll service revenues.
512. Toll private line services.	
516. Other toll service revenues.	
III. MISCELLANEOUS REVENUES.	III. MISCELLANEOUS REVENUES.
521. *Telegraph commissions.*	520. Miscellaneous operating revenues.
523. Directory advertising and sales.	
524. Rent revenues.	
525. Revenues from general services and licenses.	
526. Other operating revenues.	
IV. UNCOLLECTIBLE REVENUES.	IV. UNCOLLECTIBLE REVENUES.
530. Uncollectible operating revenues—Dr.	530. Uncollectible operating revenues—Dr.

OPERATING REVENUE ACCOUNTS

(Note particularly instructions 4, 5, 6, 50, 51, and 52)

I. LOCAL SERVICE REVENUES

500. Subscribers' station revenues.—This account shall include local service revenues from business and residence subscribers' service and from semipublic service, including such revenues

from main stations, private branch exchange systems, order turrets, and other subscribers' stations, whether the charge is based upon a flat rate or a measured rate. It shall include local service revenues from mileage charges and auxiliary equipment in connection with such subscribers' service. This account shall include also revenues from directory listings for such subscribers' service requirements, such as listings of extra names and alternate call numbers in the alphabetical sections of directories.

NOTE A.—Local service revenues from public telephones and from service stations shall be credited to accounts 501 and 503, respectively.

NOTE B.—Revenues from advertising in directories (i. e., other than listings for service requirements) shall be credited to account 523.

501. **Public telephone revenues.**—This account shall include local service revenues from public telephone service.

NOTE A.—Local service revenues from semipublic service shall be credited to account 500.

NOTE B.—Public telephone commissions shall be charged to account 648.

503. **Service stations.**—This account shall include local service revenues from stations the lines or equipment of which are provided wholly or in part by others and to which the company furnishes local service, switching service, or both.

504. **Local private line services.**—This account shall include local service revenues from private line services and facilities furnished between points in the same local service area under contracts providing exclusive service, either continuously or during stated periods (i. e., service not requiring central office switching operations). It shall include local private line service revenues from lines furnished for such purposes as telephone, telegraph, teletypewriter, public address, radio program transmission, and remote control. It shall include also charges for toll terminals and local loops furnished either continuously or during stated periods in connection with toll services (including those furnished for use in connection with lines of other companies); and charges for instruments and equipment, when furnished in connection with such lines and loops.

506. **Other local service revenues.**—This account shall include all local service revenues not provided for elsewhere.

II. TOLL SERVICE REVENUES

510. **Message tolls.**—(A) This account shall include toll service revenues from the transmission of messages, including such revenues from messages transmitted entirely over the company's own lines, and amounts representing divisions of toll service revenues received, (*a*) from messages transmitted partly over the company's lines and partly over lines of other companies, (*b*) as compensation for originating or terminating toll messages of other companies, and (*c*) as compensation for switching toll messages between lines of other companies.

(B) This account shall include revenues from guarantees at toll stations and from messenger service in notifying persons of toll calls.

512. **Toll private line services.**—This account shall include toll service revenues from private line services and facilities furnished between different local service areas under contracts providing exclusive service either continously or during stated periods, including, (*a*) revenues from services involving only the use of the company's own lines, and (*b*) amounts representing divisions of toll private line service revenues when such service involves the use of lines of other companies. It shall include toll private line service revenues from lines furnished for such purposes as telephone, telegraph, teletypewriter, public address, radio program transmission, and remote control.

NOTE A.—Charges for local loops furnished either continuously or during stated periods and the instruments used in connection therewith (including those furnished for use in connection with lines of other companies) shall be credited to account 504.

NOTE B.—Toll service revenues from the transmission of messages charged for on a per-message basis shall be included in account 510.

516. **Other toll service revenues.**—This account shall include all toll service revenues not provided for elsewhere.

III. MISCELLANEOUS REVENUES

521. **Telegraph commissions.**—This account shall include commissions receivable for the billing or collection of telegraph, cable, or wireless tolls on messages transmitted by others.

523. **Directory advertising and sales.**—This account shall include revenues from advertising in directories, and from the sale or furnishing of new directories either of the company's own issue or directories purchased from others. It shall include all revenues from the classified sections and from bold-face listings, marginal displays, inserts, cover and other advertisements in alphabetical sections of directories.

NOTE A.—Revenues from directory listings for service requirements, such as listings of extra names and alternate call numbers in the alphabetical sections of directories, shall be credited to account 500.

NOTE B.—Revenues from advertising other than in directories shall be credited to account 526.

NOTE C.—Amounts received as salvage on old directories shall be credited to account 649.

524. **Rent revenues.**—This account shall include revenues, including taxes when borne by the lessee, from the rental or subrental to others of telephone plant constituting a part of the property used by the company in its telephone operations, such as instruments, equipment, and lines furnished apart from telephone service (note instruction 3–AA) rendered by the company; space in conduits; pole line space for attachments; space in buildings; and carrying charges on property used in joint operations (see also instruction 62 and note B to this account).

NOTE A.—The expenses of maintaining and operating the rented property, including depreciation and insurance, shall be included in the appropriate operating expense accounts. Taxes applicable to the rented property shall be included by the owner of the rented property in account 308.

NOTE B.—Rents from the exclusive use of telephone operating property held as a whole and operated by others such as a complete telephone plant, a complete exchange, or a complete toll system, shall be included in account 302.

525. **Revenues from general services and licenses.**—This account shall include amounts accruing for services rendered other companies under a license agreement, general service contract, or other arrangement providing for the furnishing of general accounting, engineering, financial, legal, patent, and other general services.

526. **Other operating revenues.**—This account shall include all miscellaneous operating revenues not provided for elsewhere, such as amounts charged for private branch exchange operating services performed by operators regularly employed by the telephone company; flat amounts (not divisions of revenue or reimbursements of costs) charged other telephone companies for operating services on toll lines of such companies terminating in the switchboard of the accounting company; revenues from advertising other than in directories; unclaimed refunds or overcharges on telephone service; and profits realized from custom work performed for others incident to the company's telephone operations.

IV. UNCOLLECTIBLE REVENUES

530. **Uncollectible operating revenues—Dr.**—(A) This account shall include amounts credited to the operating revenue accounts which have proved impracticable of collection. (See also instruction 11 and account 118–B.)

(B) This account may include monthly charges based on estimates, to provide a reserve for uncollectible accounts due from customers and agents. Amounts thus charged to this account shall be credited to subaccount (B), "Reserve for uncollectible accounts—Cr.," under account 118, "Due from customers and agents."

(C) When revenue which has been written off through this account is collected, the amount of the collection shall be credited to this account.

NOTE.—Uncollectible amounts which have not been treated as operating revenues shall be charged to account 323, account 413, or other appropriate account.

OPERATING EXPENSE ACCOUNTS

ACCOUNTS FOR CLASS A COMPANIES

I. MAINTENANCE EXPENSES.
- 602. Repairs of outside plant.
- 604. Repairs of central office equipment.
- 606. Repairs of station equipment.
- 608. Repairs of buildings and grounds.

ACCOUNTS FOR CLASS B COMPANIES

I. MAINTENANCE EXPENSES.
- 602. Repairs of outside plant.
- 604. Repairs of central office equipment.
- 606. Repairs of station equipment.
- 608. Repairs of buildings and grounds.

ACCOUNTS FOR CLASS A COMPANIES—Continued.

I. MAINTENANCE EXPENSES—Contd.
- 607. Station removals and changes.
- 608. Depreciation.
- 609. Extraordinary retirements.
- 610. Maintaining transmission power.
- 611. Employment stabilization.
- 612. Other maintenance expenses.

II. TRAFFIC EXPENSES.
- 621. General traffic supervision.
- 622. Service inspection and customer instruction.
- 624. Operators' wages.
- 626. Rest and lunch rooms.
- 627. Operators' employment and training.
- 629. Central office stationery and printing.
- 630. Central office house service.
- 631. Miscellaneous central office expenses.
- 632. Public telephone expenses.
- 633. Other traffic expenses.
- 634. Joint traffic expenses—Dr.
- 635. Joint traffic expenses—Cr.

III. COMMERCIAL EXPENSES.
- 640. General commercial administration.
- 642. Advertising.
- 643. Sales expense.
- 644. Connecting company relations.
- 645. Local commercial operations.
- 648. Public telephone commissions
- 649. Directory expenses.
- 650. Other commercial expenses.

IV. GENERAL OFFICE SALARIES AND EXPENSES.
- 661. Executive department.
- 662. Accounting department.
- 663. Treasury department.
- 664. Law department.
- 665. Other general office salaries and expenses.

V. OTHER OPERATING EXPENSES.
- 668. Insurance.
- 669. Accidents and damages.
- 671. Operating rents.
- 672. Relief and pensions.
- 673. Telephone franchise requirements.
- 674. General services and licenses.
- 675. Other expenses.
- 676. Telephone franchise requirements—Cr.
- 677. Expenses charged construction—Cr.

ACCOUNTS FOR CLASS B COMPANIES—Continued.

I. MAINTENANCE EXPENSES—Contd.
- 607. Station removals and changes.
- 608. Depreciation.
- 609. Extraordinary retirements.
- 610. Maintaining transmission power.
- 611. Employment stabilization.
- 612. Other maintenance expenses.

II. TRAFFIC EXPENSES.
- 624. Operators' wages.
- 633. Other traffic expenses.

III. COMMERCIAL EXPENSES.
- 640. Commercial expenses.

IV. GENERAL OFFICE SALARIES AND EXPENSES.
- 665. General office salaries and expenses.

V. OTHER OPERATING EXPENSES.
- 675. Other operating expenses.

OPERATING EXPENSE ACCOUNTS

(Note particularly instructions 4, 5, 6, 25, and 60 to 64, inclusive)

II. MAINTENANCE EXPENSES

602. Repairs of outside plant.—This account shall include the cost of repairing pole lines, cable, aerial wire and underground conduit, and the cost of maintaining right of way for such plant.

ITEMS

[Note instruction 8]

Cleaning manholes and ducts. (See also note A to this account.)
Clearing defective cable pairs.
Cutting out or cutting in slack in aerial wire.
Inspecting, testing, and reporting on the condition of outside plant to determine need for repairs or replacements.
Installing, transferring, replacing, and removing cross-connection wires and fuses in cable terminals or boxes. (See also note B to this account.)
Moving poles, wires, cables, and other outside plant in connection with road and street changes. (See also instruction 25.)
Opening pavement and repaving in connection with repairs of outside plant.
Opening, testing, splicing, and other work of transferring pairs in cable and transferring cable from one cable or stub to another cable or stub.
Painting and creosoting poles and pole butts subsequent to their installation.
Permits and privileges for maintenance work.
Rearranging wires on pins.
Repairing used outside plant material for reuse.
Replacing minor items of outside plant including labor and material used and the removal and recovery of the items retired less salvage recovered, except when such items are replaced through the replacement of units of property. (See also instruction 25.)
Reracking cables.
Respacing poles and crossarms.
Restoring condition of outside plant damaged by storms, fires, or other casualties. (See also instruction 25.)
Right of way adjustments, cost of, when no additional rights are secured.
Straightening poles and crossarms.
Testing for, locating and clearing trouble.
Tests and surveys of existing plant to detect presence of electrolysis. (See also note C to this account.)
Tightening guys and raking guy stubs.
Tightening suspension strand and cutting out cable slack.
Transferring crossarms, guys, wires, cables, cable boxes, and other outside plant in connection with replacements of poles and crossarms.
Transposing or retransposing existing aerial wire, including such work for the removal of electrical interference and for the creation of phantom and carrier circuits subsequent to the original installation of the wires. (See also note D to this account.)
Trenching poles.
Trimming trees, cutting underbrush, and other work to maintain previous clearance of right of way.
Work on the property of others in connection with the maintenance of oustide plant of the accounting company. (See also note E to this account.)

NOTE A.—The cost of cleaning manholes and ducts in connection with construction work and not necessary in the maintenance or operation of the plant shall be included in the account chargeable with the cost of the construction work.

NOTE B.—The cost of cross-connection wires and fuses installed in the first equipment for service of cable terminals or boxes shall be charged to account 242.

NOTE C.—The cost of tests for electrolysis made in the course of construction shall be included in the cost of the cable installed.

NOTE D.—The cost of any betterments and plant added resulting from such work shall be included in the appropriate telephone plant accounts.

NOTE E.—Expenses on account of property of others damaged in connection with maintenance work, except for the cost of incidentally repairing property of others in the course of such work, shall be charged to account 669.

NOTE F.—The cost of repairing drop and block wires shall be charged to account 605.

604. **Repairs of central office equipment.**—(A) This account shall include the cost of repairing central office equipment.

(B) This account shall include also the pay and expenses of plant department forces engaged in maintaining and operating equipment for producing electricity for transmitting traffic and operating signals.

ITEMS

[Note instruction 8]

Adding acid and water to batteries and reading specific gravity, current drain and voltage of batteries.
Cleaning equipment.
Disconnecting and reconnecting customers' lines in central offices for temporary periods of nonuse or for nonpayment of bills.
Disconnecting customers' lines in central offices due to termination of service.
House service. (See also account 707.)
Lubrication, adjustment, and cleaning of power equipment, including the lubrication and cleaning of drive motors and driving mechanism in panel offices.
Operating prime movers, generators, and motors.
Rearranging and replacing frame cross-connection wires. (See also note A to this account.)
Regulating power for repeaters.
Removing sediment from storage batteries and the cost of repairing storage batteries, including replacements of minor items.
Repairing used central office equipment for reuse.
Replacement of central office dry cell batteries.
Replacing minor items of central office equipment including labor and material used and the removal and recovery of the items retired less salvage recovered, except when such items are replaced through the replacement of units of property. (See also instruction 25.)
Starting, stopping, and watching operation of power equipment.
Supplies, such as acid, caustic soda, cheese cloth, commutator paste, dry cells, electrolyte, kerosene, oil, and waste.
Testing for, locating, and clearing trouble. (See also note B to this account.)
Tools and other individual central office equipment—items of small value or short life, cost and repairs of. (See also instruction 20-E.)
Training employees for central office repair work.
Underlining switchboard jacks, renewing switchboard markings, and placing and changing number plates, and designation strips not incident to construction. (See also note C to this account and instruction 63.)
Watching and regulating the operation of repeaters, duplex and multiplex apparatus on telephone and telegraph lines.

NOTE A.—The cost of work on central office frames incident to routine station and line turnover and growth, including the placing, removing, or rearrangement of cross connections (including the cost, less salvage, of the cross connection wire, heat coils, protector blocks, etc.), and the opening and closing of lines on the frame, may be currently charged direct to this account and, before the close of the calendar year, adjustment made between this account and account 221 for the net increase in central office investment or between account 221 and account 171 for the net decrease in such investment, due to increase or decrease in lines.

NOTE B.—The pay and expenses of test-board men and other employees in central offices engaged in testing circuits in plant outside of central offices, testing with station repairmen, installers, etc., shall be included in the appropriate maintenance and tele-

phone plant accounts according to the class of plant tested and the nature of the work involved. (See also instruction 63.)

NOTE C.—The pay of clerks of the traffic department when engaged in such work shall be charged to account 624. The cost of placing number plates, designation strips, making switchboard markings, and similar work in connection with central office construction shall be included in account 221. (See also instruction 63.)

NOTE D.—The cost of power produced for house service purposes shall be charged to account 707 or other account, as may be appropriate.

NOTE E.—The cost of electricity purchased and the cost of coal, gas, gasoline, oil and other fuel used in the generation, conversion, and storage of current for transmitting traffic and operating signals shall be included in account 610.

605. **Repairs of station equipment.**—(A) This account shall include the cost of repairing station apparatus, station installations (including inside wires), drop and block wires, private branch exchanges and booths, and special fittings.

(B) This account shall include also such costs of extensive replacements of station apparatus and inside, drop, and block wires, which, under conditions provided in Instruction 64, have been carried in suspense in account 138, "Extraordinary maintenance suspense."

ITEMS

[Note instruction 8]

Changing type of station apparatus, such as from desk set to hand set, wall set to desk set, magneto to common battery, or nondial to dial. (See also note A to this account.)

Changing drop wires from street to alley or interior block distribution, together with associated changes of inside wires.

Cleaning equipment.

Inside moves (moves or relocations on the same premises or at the same address) of station apparatus, private branch exchanges and booths, and special fittings (See also note B to this account.)

Inspecting, testing, and reporting on condition of equipment to determine need for repairs or replacements.

Labor, traveling, and other incidental costs of replacing any items (including "units of property") of station apparatus. (See also note A to this account.)

Material used in replacing minor items of station apparatus. (See also instruction 25.)

Number plate changes not incident to station reconnections.

Relocating inside, drop, and block wires.

Removing sediment from and cleaning private branch exchange batteries.

Repainting and other repairs of booths, including those owned by others.

Repairing used station equipment for reuse.

Repairing furniture and equipment classified to account 235 and cost and repairs of individual items of small value or short life. (See also instruction 20–E.)

Replacing minor items of private branch exchanges and booths and special fittings, including labor and material used and the removal and recovery of the items retired less salvage recovered, except when such items are replaced through the replacement of units of property. (See also instruction 25.)

Replacing inside, drop, and block wires.

Replacing station batteries.

Retirement (book cost, plus cost of removal less salvage recovered) of drop or block wires, in the course of extensive plant rearrangements, such as the replacement of such wires by cable.

Routine work to prevent trouble, such as trimming trees to protect existing drop wires.

Testing for, locating, and clearing trouble in station equipment.

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NOTE A.—The cost of plant added (such as dials) or betterments of station apparatus shall be charged to account 231. When a "unit of property" (see also instructions 24 and 25) of station apparatus is replaced, account 231 shall be charged with the cost of the material installed and credited with the cost of the material retired; the latter amount less the value of salvage recovered shall be charged to account 171.

NOTE B.—Moves of stations, private branch exchanges and booths, and special fittings to different premises or to a different address shall be accounted for as removals or disconnections, as appropriate, from the old location, and as new installations, reinstallations, or reconnections, as appropriate, at the new location. (See also account 607.)

NOTE C.—Amounts charged customers for moves and changes of station equipment shall be credited to account 500 or to other revenue accounts appropriate for the class of service involved.

606. **Repairs of buildings and grounds.**—This account shall include the cost of repairing buildings and grounds, their fixtures and appurtenances, except as provided in the texts of the clearing accounts in respect to rented quarters.

ITEMS

[Note instruction 8]

Changing location of partitions. (See also note A to this account.)

Maintaining public improvements, including assessments covering such work.

Maintaining yards and grounds, including their fences, shrubbery, sidewalks, and sewers.

Minor improvements to leased buildings, quarters, and grounds. (See also instruction 23.)

Repainting and repapering buildings, including redecorating interiors of buildings.

Repairing building machinery, fixtures, appurtenances, and appliances, such as elevators, plumbing, and equipment for heating, lighting, and ventilating.

Repairing rented buildings, quarters, and grounds, except when the rented property is used in operations the expense of which is chargeable to the clearing accounts.

Replacing and repairing awnings, screens, window shades and ventilators, storm doors, storm windows, movable partitions, and similar movable minor items of buildings. (See also note B to this account.)

Replacing minor items of buildings, including labor and material used and the removal and recovery of the items retired less salvage recovered, except when such items are replaced through the replacement of units of property. (See also instruction 25 and note C to this account.)

Restoring condition of buildings or grounds damaged in the course of repairs, replacements, additions, or betterments. (See also note C to this account.)

NOTE A.—The cost of any substantial increase or decrease in partitions resulting from such changes shall be charged or credited, as appropriate, to account 212.

NOTE B.—When partitions of a movable type (for example, steel and glass, or wood and glass) are replaced by partitions of a permanent type (for example, terra cotta) or vice versa, the costs involved shall be accounted for through the telephone plant and depreciation reserve accounts.

NOTE C.—The cost of minor building alterations incident to the installation of central office equipment, such as opening and closing holes in ceilings, partitions, walls and floors to permit installation of equipment, power conduit and wiring, shall be charged to account 221.

NOTE D.—The cost of initial improvements (including repairs, rearrangements, plant added and betterments) in the preparation for service of either rented or purchased buildings or grounds shall be charged to account 211 or account 212, as appropriate, except that when the improvements to leased property are of relatively minor cost or short life or the period of the lease is less than one year, the cost shall be charged to the account chargeable with the cost of repairs of such property. (See also instruction 23.)

NOTE E.—The cost of repairs to buildings and grounds classable under account 103 shall be charged to account 315.

607. **Station removals and changes.**—(A) This account shall include the expense of removing stations due to the termination of service together with the resultant loss of investment in station installations, drop and block wires, and the expense of station disconnections, reconnections, and reinstallations, as follows:

(B) When stations are removed from subscribers' premises, the original cost (actual or estimated average unit cost) of the station installations (including inside wires) carried in account 232, "Station installations," and of any drop and block wires thereby retired from service, shall be credited to the appropriate telephone plant accounts and charged to this account, which shall be credited with the value of any salvage recovered therefrom. The cost of removing the station apparatus, inside, drop and block wires, including transportation costs incurred in the recovery of the material, shall be charged to this account.

(C) When stations are disconnected but left on premises (either for nonpayment or other discontinuance of service) this account shall be charged with the cost of disconnecting the station equipment; and when reconnected, the cost of reconnecting shall also be charged hereto.

(D) When stations are reinstalled on premises from which the station apparatus had previously been removed, if inside wire or ground wire left from a previous installation is reused, wholly or in part, the cost of installing the station apparatus (not including the cost of the apparatus which shall be charged to account 231) and of placing the inside wire again in service shall be charged to this account, and this account shall be credited and account 232, "Station installations," charged with the average cost of a station installation (including inside wire) in place; if drop or block wire left from a previous installation is reused, wholly or in part, the cost of placing such wire again in service shall be charged to this account, and this account shall be credited and account 233, "Drop and block wires," charged with the average cost of a drop or block wire in place.

NOTE A.—The cost of disconnecting and reconnecting subscribers' lines in central offices shall be charged to account 604.

NOTE B.—Amounts charged subscribers for restoration of service shall be credited to account 500 or to other revenue accounts appropriate for the class of service involved.

608. **Depreciation.**—This account shall include the amount of depreciation charges applicable to the accounting period for all classes of depreciable telephone plant, except for plant classified in account 264, "Vehicles and other work equipment." The depreciation charges shall be made in accordance with instructions 23–C, 80, 81, and 82. (See accounts 315 and 174 for depreciation of miscellaneous physical property.)

609. **Extraordinary retirements.**—This account shall include the proportion of the service value of telephone plant retired, carried in account 138, "Extraordinary maintenance suspense," which by specific authority of this Commission shall be charged to

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operating expenses for the period. (See also instruction 83 and par. (A) of account 138.)

610. **Maintaining transmission power.**—This account shall include the cost of power of transmitting traffic and operating signals. It shall include the cost of electricity purchased and the cost of coal, gas, gasoline, oil and other fuel used in the generation, conversion and storage of current for operating dial system, repeater, and carrier equipment, ringing machines, ticket distributor systems, battery charging machines, coin collection equipment, and for other transmission power requirements of central office equipment, private branch exchanges, and other station equipment.

NOTE A.—Payments for the installation in central offices of permanent power circuits for emergency use shall be charged to the appropriate plant account. Payments to others made with a provision for reimbursement as power is used shall be treated as a prepayment and cleared by charges to this account or other appropriate account.

NOTE B.—The cost of power produced for house service purposes shall be charged to account 707 or other account as may be appropriate.

NOTE C.—The pay and expenses of central office forces engaged in the generation, conversion, and regulation of transmission power shall be charged to account 604.

611. **Employment stabilization.**—(A) This account shall include amounts systematically accrued in respect of maintenance work to be performed in accordance with an employment stabilization program designed to spread the total volume of maintenance work more evenly from year to year. Charges to this account shall be made only after approval by this Commission of the company's employment stabilization program, the plan of administration of the program, the character of the work to which sums accrued may subsequently be applied and the amount of the monthly or annual accruals for stabilization purposes.

(B) Amounts charged to this account shall concurrently be credited to account 173, "Employment stabilization reserve."

(C) When maintenance work for which provision has been made through this account is performed, the cost of such work shall be charged to and included in the appropriate maintenance expense accounts. Concurrently, this account shall be credited and account 173, "Employment stabilization reserve," shall be charged with an amount equal to the cost of such work.

612. **Other maintenance expenses.**—This account shall include all maintenance expenses not properly chargeable to other accounts.

II. TRAFFIC EXPENSES

621. **General traffic supervision.**—This account shall include the pay, office, traveling, and other expenses of officers directly in charge of the general supervision of traffic, either for the company as a whole or a territorial subdivision; also the pay and expenses of their assistants and office forces.

ITEMS

[Note instruction 8]

House service. (See also account 707.)
Medical examiners and their assistants, welfare supervisors, and nurses engaged in the traffic department, pay and expenses of. (See also note A to this account.)
Office supplies.
Postage, printing, and stationery.
Preparing tariff and route data, traffic department's expense of. (See also note B to this account.)
Repairs of furniture and office equipment and cost and repairs of individual items of small value or short life.
Traffic superintendents, managers, chiefs, supervisors, and engineers, pay and expenses of. (See also note C to this account.)
Traveling expenses.

NOTE A.—The pay and expenses of physicians and nurses engaged in work such as conducting physical examinations of employees for all departments, giving general health advice, providing first-aid treatment, supervising and investigating sickness cases, and in other general relief activities shall be charged to account 672. The pay of nurses assigned to operators' quarters shall be charged to account 626.

NOTE B.—The traffic department's proportion of the expense of printing and distributing tariff and route data shall be charged to account 629.

NOTE C.—The cost of traffic engineering applicable to construction shall be credited to this account.

622. **Service inspection and customer instruction.**—(A) This account shall include the pay, and office, traveling, and other expenses of service observation forces. It shall include also the expense of inspecting and directly supervising private-branch-exchange service.

(B) This account shall also be charged with the expense of instructing customers in methods of placing calls, including instruction in the use of dial equipment. (See also note A to this account.)

ITEMS

[Note instruction 8]

Card notices and other literature for instruction of customers in use of dial equipment.
Employment and training of private-branch-exchange operators apart from the regular employment and training of operators.
House service. (See also account 707.)
Investigation and adjustment to traffic service complaints. (See also note B to this account.)
Making test calls.
Observation of handling of traffic by operators. (See also note C to this account.)
Observation of accuracy of measured service charges.
Office supplies.
Postage, printing, and stationery.
Private-branch-exchange service supervisors, pay and expenses of.
Repairs of furniture and office equipment and cost and repairs of individual items of small value or short life.
Stop watches, repairs of.
Summarization of service observation data.
Traveling expenses.

NOTE A.—The expense of instructing customers in the use of station equipment in the course of station installation activities shall be included in the accounts charged with the cost of such activities.

NOTE B.—The recording and adjustment of traffic service complaints performed by operating forces in the course of completing calls shall be included in account 624.

NOTE C.—The pay of operators, supervisors, and other employees in central office operating rooms engaged in listening-in work in connection with coaching operators shall be charged to account 624.

624. **Operators' wages.**—(A) This account shall include the pay of chief operators, assistant chief operators, monitors, supervisors, ticket distributors, switchboard operators, information operators, directory operators, private-branch-exchange operators, telegraph operators, teletypewriter operators, operators employed in quoting toll rates and charges, listening-in work in connection with coaching operators, helping subscribers to place and complete calls together with the incidental recording of subscribers' complaints, operating telephotographic equipment, and all other operators employed in the operation of central-office and private-branch-exchange equipment.

(B) This account shall include also the pay of clerks, stenographers, and messengers engaged in line assignments, peg counts, message register readings, plug counts, preparing time or attendance records, payrolls, intercepting records, panel and jack records, line and station reports, delivering messages or notifying persons of calls, and similar traffic work performed in central offices or centralized outside of central offices. It shall include the pay of such employees while engaged in underlining switchboard jacks and placing and changing number plates and designation strips.

NOTE A.—The pay of operators at public telephone stations shall be charged to account 632.

NOTE B.—Commissions or agency contract allowances paid to exchange agents or managers in lieu of salary, operating expenses, etc., shall be equitably apportioned to construction, maintenance, traffic, commercial, or other accounts affected.

NOTE C.—The pay and expenses of operators, supervisors, chief operators, etc., while attending supplemental training or post-graduate operating schools shall be charged to account 627.

626. **Rest and lunch rooms.**—This account shall include the cost of operating rest and lunch rooms for central office employees, including the cost of meals provided for such employees. This includes the cost of operating such facilities as rest rooms, quiet rooms, reading rooms, medical rooms, locker rooms, check rooms, sleeping rooms, and dormitories. Credit to this account amounts received for meals served.

ITEMS

[Note instruction 8]

Bedding.
Dishes.
Electric power for cooking, refrigeration, or operating kitchen equipment.
Food supplies.
Fuel for cooking.
Handling orders and bills for supplies.
House service. (See also account 707.)
Ice for refrigeration.
Laundry.
Linen.

Lunch-room managers, cooks, cashiers, waiters, and kitchen helpers, pay and expenses of.
Medical supplies, including first-aid materials, used in operators' quarters.
Newspapers, magazines, and phonograph records.
Nurses, matrons, and attendants for operators' quarters, pay and expenses of.
Postage, printing, and stationery.
Repairs of furniture and equipment and cost and repairs of individual items of small value or short life.
Silverware.
Uniforms.

NOTE.—The net cost of operating central office rest and lunch rooms used, except incidentally, by other than employees of the traffic department shall be apportioned on an equitable basis to the departments benefited.

627. **Operators' employment and training.**—This account shall include expenses incurred in the employment and training of operators whether or not a school is maintained.

ITEMS

[Note instruction 8]

Advertising for operators, cost of.
Amounts paid employees for securing new operators.
Pay and expenses of employees engaged in the employment of operators and in interviewing applicants.
Pay and expenses of instructors, messengers, personnel supervisors, etc., in schools.
Pay of operators, supervisors, chief operators, etc., attending supplemental training or post-graduate courses.
Pay of student operators rendering no service.
Postage, printing, and stationery.
Repairs of furniture and office equipment and cost and repairs of individual items of small value or short life.
Supplies for employment and school work.
Traveling expenses.

NOTE.—The cost of house service for operators' schools shall be charged to account 630. (See also account 707.)

629. **Central office stationery and printing.**—This account shall include the cost of postage, printing, and stationery for use in central offices except as provided for elsewhere.

ITEMS

[Note instruction 8]

Office supplies.
Postage on toll tickets forwarded by connecting companies.
Postage on toll tickets from central offices to accounting offices.
Printing and distributing tariff and route data, traffic department's proportion of cost of. (See also note A to this account.)
Printing directories of telephone numbers by street addresses, traffic department's expense of. (See also note B to this account.)
Tickets and other central office stationery and supplies furnished connecting companies.
Toll tickets.

NOTE A.—The expense of preparing tariff and route data incurred by the traffic department shall be charged to account 621.

NOTE B.—The cost of such directories prepared by the directory department shall be charged to account 649.

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630. **Central office house service.**—This account shall include the cost of light, heat, janitor service, and other care of central office traffic quarters except as provided in account 626, "Rest and lunch rooms." (See also account 707.)

ITEMS

[Note instruction 8]

Electricity for elevators, fans, lights, and ventilators. (See also note A to this account.)

Fuel, ice, towels, water, toilet, and other supplies.

NOTE A.—The cost of electricity used in connection with central office equipment installations shall be charged to account 221.

NOTE B.—The cost of house service for central office plant quarters shall be charged to account 604 or to an appropriate clearing account.

631. **Miscellaneous central office expenses.**—This account shall include the cost of operating central offices not chargeable to other accounts.

ITEMS

[Note instruction 8]

Board and lodging for operators.

Carfare and cabfare for divided tour operators.

Clothing furnished operators in emergencies.

Films for message register readings.

Laundry of equipment used by operators.

Messenger service. (See also note A to this account.)

Paint brushes, paint, and other articles used by traffic employees in switchboard markings.

Photographic supplies for telephotographic work.

Rent of typewriters for central offices.

Repairs of furniture and office equipment and cost and repairs of individual items of small value or short life used in central office operating quarters. (See also note B to this account.)

Time service furnished the company by others.

Traveling expenses of employees whose pay is chargeable to account 624.

NOTE A.—The pay of company employees engaged in central office messenger service shall be charged to account 624.

NOTE B.—Repairs of furniture and office equipment and the cost and repairs of individual items of small value or short life used in central office plant quarters shall be charged to account 604, or to an appropriate clearing account. Such costs for items used in rest and lunch room quarters shall be charged to account 626, and those for items used in operators' employment and school quarters shall be charged to account 627.

632. **Public telephone expenses.**—This account shall include all traffic expenses, except central office operating expenses, incurred in connection with the operation of public telephones.

ITEMS

[Note instruction 8]

Attendants, clerks, messengers, and operators at public telephones, pay and expenses of.

Employees engaged in direct supervision of the operation of public telephone service, pay and expenses of.

House service. (See also account 707.)

Instruction cards for booths.

Postage, printing, and stationery.

Traveling expenses.

Uniforms.

NOTE.—Commissions, percentages of receipts, and flat sums paid for occupancy privileges for public telephones shall be charged to account 648.

633. **Other traffic expenses.**—This account shall include all traffic expenses not properly chargeable to other accounts.

NOTE A.—Rent paid for central offices shall be charged to account 671.

NOTE B.—Traffic expenses incurred in the operation of special-type equipment, such as public-address systems, telephotographic, radio broadcasting, and receiving, motion-picture and public-demonstration equipment, shall be charged, so far as practicable, to the traffic expense accounts provided for the expenses of regular telephone operations.

634. **Joint traffic expenses—Dr.**—This account may include amounts payable to other telephone companies for joint traffic expenses, as provided in instruction 62.

635. **Joint traffic expenses—Cr.**—This account may include amounts receivable from other telephone companies for joint traffic expenses, as provided in instruction 62.

III. COMMERCIAL EXPENSES

640. **General commercial administration.**—This account shall include the pay, office, traveling, and other expenses of officers directly in charge of the general administration of the commercial department either for the company as a whole or a territorial subdivision; also the pay and expenses of their assistants and office forces.

ITEMS

[Note instruction 8]

Commercial surveys, forecasts, rate-plan studies, and development studies. (See also note B to this account.)
General, division, and district commercial managers, supervisors, superintendents, and engineers, pay and expenses of. (See also notes A and B to this account.)
House service. (See also account 707.)
Office supplies.
Postage, printing, and stationery.
Preparing, printing, and distributing tariff and route data, commercial department's expense of.
Repairs of furniture and office equipment and cost and repairs of individual items of small value or short life.
Traveling expenses.

NOTE A.—The pay and expenses of an employee engaged in direct supervision of commercial activities the cost of which is provided for in specific accounts, such as a manager in direct charge of local commercial operations, an advertising manager, a supervisor in direct charge of a group of salesmen, a directory manager, or a representative in charge of connecting company relations shall be charged to the account or accounts provided for such costs.

NOTE B.—The cost of commercial engineering applicable to construction shall be credited to this account.

642. **Advertising.**—This account shall include expenses incurred in commercial advertising activities, including expenses incurred in giving public demonstrations of telephones, switchboards, etc.

ITEMS

[Note instruction 8]

Announcements to customers in regard to proposed or other rate changes. (See also note A to this account.)
Commercial advertisements in newspapers and magazines. (See also note A to this account.)
Commercial advertising matter such as posters, bulletins, booklets, and related items. (See also note A to this account.)
Electric current consumed in illuminating public telephone signs.
Exhibits in connection with industrial expositions, expenses of. (See also note B to this account.)
House service. (See also account 707.)
Lecture and demonstration tours for promotion purposes. (See also note B to this account.)
Managers and their office forces in charge of advertising and publicity, pay and expenses of.
Motion pictures.
Office supplies.
Postage, printing, and stationery.
Promotional advertising in the company's directories, such as colored page inserts, when additional printing and binding costs are incurred.
Radio programs.
Repairs of furniture and office equipment and cost and repairs of individual items of small value or short life.
Traveling expenses.
Window displays.

NOTE A.—The cost of newspaper advertisements, literature, etc., other than for commercial advertising purposes, such as advertisements of stock and bond issues, advertising for operators, notices of dividends declared, and advertisements for sale of directory advertising or to popularize and increase use of classified sections of directories, shall be charged to the accounts appropriate for such costs.

NOTE B.—The pay and expenses of employees performing incidental services in connection with industrial exhibits and public demonstrations of telephones, switchboards, etc., shall be included in the accounts chargeable with the pay and expenses of the employees' regular activities. (See also instruction 63.)

NOTE C.—The cost of flags, bunting, and similar expenses of decorating buildings shall be charged to account 707 or to the appropriate expense account of the department concerned.

643. **Sales expense.**—This account shall include expenses incurred in canvassing for new business or for changing or renewing existing service, also in interviewing customers for promoting the further use of service.

ITEMS

[Note instruction 8]

Canvassers and salesmen, pay and expenses of. (See also note to this account.)
Canvassing for purpose of regrading service or for sale of additional service.
Commercial service studies of subscribers' service.
House service. (See also account 707.)
Office supplies.
Postage, printing, and stationery.
Repairs of furniture and office equipment and cost and repairs of individual items of small value or short life.
Traveling expenses.

NOTE.—The pay and expenses of employees engaged in securing advertisements for directories shall be charged to account 132 or account 649, as may be appropriate.

644. **Connecting company relations.**—This account shall include expenses incurred in developing the interchange of business and

other promotion of relations with connecting companies. This includes the pay and expenses of commercial representatives and their office forces engaged in the negotiation or revision of traffic agreements, assisting connecting companies in the development of toll business and similar promotion of relations with connecting companies.

ITEMS

[Note instruction 8]

Connecting company agents or representatives and their office forces, pay and expenses of.
House service. (See also account 707.)
Office supplies.
Postage, printing, and stationery.
Repairs of furniture and office equipment and cos and repairs of individual items of small value or short life.
Traveling expenses.

645. **Local commercial operations.**—This account shall include the pay, office, traveling and other expenses of employees engaged in local commercial operations other than promotion or directory. This includes employees of business and collection offices engaged in preparing, changing and handling contract or service orders, collecting revenue and handling miscellaneous commercial relations with customers.

ITEMS

[Note instruction 8]

Badges.
Business office signs on windows, doors, etc.
Coin box collectors, guards and supervisors of coin box collections, pay and expenses of.
Customers' accounts, cost of keeping and billing, when performed in the course of local commercial operations. (See also note C to this account.)
Fees paid banks or others for collection of customers' bills. (For law expenses see account 664.)
House service. (See also account 707.)
Managers in charge of local commercial operations, supervisors, counter men, bookkeepers, cashiers, clerks, and collectors, pay and expenses of. (See also note C to this account.)
Office supplies.
Postage, printing, and stationery.
Repairs of furniture and office equipment and cost and repairs of individual items of small value or short life.
Traveling expenses.

NOTE A.—This account shall include the entire pay and expenses of employees in business offices who are only incidentally engaged in promotion or directory work. If such employees are assigned all or a part of their time to promotion or directory work equitable portions of their pay and expenses shall be charged to the accounts provided for such expenses. (See also instruction 63.)

NOTE B.—The cost of duplicating, recording and handling contract or service orders after preparation by the commercial department shall be charged to the accounts of the department incurring the expense.

NOTE C.—When customers' accounts are kept and bills rendered by the accounting department, the expense involved, including pay and expenses of bookkeepers and clerks, shall be charged to account 662.

648. **Public telephone commissions.**—This account shall include amounts paid, either in the form of percentages of receipts, flat

amounts deducted from receipts or other specified sums, to the owners or tenants of premises upon which attended and nonattended public and semipublic telephone stations are located, as general compensation for occupancy privileges, light, heat, attendance and all services rendered incident to the furnishing of service from such stations.

NOTE.—The pay of operators and other attendants employed by the company at public telephone stations shall be charged to account 632.

649. **Directory expenses.**—This account shall include expenses incurred in preparing copy, printing, binding, and distributing directories, and the cost of securing advertisements for directories. It shall include also the cost of directories of other companies purchased for the use of the company or for distribution or sale to its customers. This account shall be credited with amounts received as salvage on old directories. (See also account 132.)

ITEMS

[Note instruction 8]

Advertisements for promotion of directory advertising.
Commissions paid employees or agents for securing directory advertisements.
Directory covers.
Directory managers, clerks, advertising salesmen, and other employees of the directory department, pay and expenses of.
House service. (See also account 707).
Maintaining directory delivery records.
Office supplies.
Official branch exchange directories prepared by directory department, cost of.
Postage, printing, and stationery.
Preparing and printing special editions of directories, including addenda thereto, by the directory department for use of traffic department. (See also note C to this account.)
Preparing and printing street address, toll and other special directories, including addenda thereto, by directory department. (See also note C to this account).
Repairs of furniture and office equipment and cost and repairs of individual items of small value or short life.
Transportation and distribution of directories, cost of.
Traveling expenses.

NOTE A.—All directory expenses may be initially charged to account 132, but shall be cleared to account 649 during the months to which such expenses apply.

NOTE B.—Receipts from the sale or furnishing of new directories, either of a company's own issue or directories purchased from others, shall be credited to account 523.

NOTE C.—When such directories are prepared and issued by the traffic department, the costs involved shall be included in the appropriate traffic expense accounts.

NOTE D.—Any additional printing and binding costs incurred on account of the company's promotional advertising in its directories, such as colored page inserts, shall be charged to account 642.

650. **Other commercial expenses.**—This account shall include all commercial expenses not properly chargeable to other accounts. It shall include any definitely known amounts of losses of revenue collections due to fire or theft, (*a*) at customers' coin-box stations, (*b*) at public or semipublic telephone stations, (*c*) in the possession

of collectors en route to collection offices, (*d*) on hand at collection offices, and (*e*) between collection offices and banks.

NOTE A.—Rent paid for commercial offices shall be charged to account 671.

NOTE B.—Commercial expenses incurred in connection with public demonstrations and such services as public address and telephotograph operations shall be charged, so far as practicable, to the commercial expense accounts provided for the expenses of regular telephone operations.

IV. General Office Salaries and Expenses

661. **Executive department.**—This account shall include the pay, office, traveling and other expenses of officers who are engaged in the general administration or management of the company, or its affairs in a territorial subdivision; also the pay and expenses of their assistants and office forces.

This account shall be charged also with salaries, fees, and expenses other than law expenses, of receivers.

Officers and Employees

[Note instruction 8]

Chairman of the board of directors.
Managers—general and division.
President.
Receiver.
Secretary.
Vice president.
Assistants authorized to act for officers of executive department.
Office and staff forces (e. g., staff assistants, secretaries, stenographers, clerks, messengers, office boys, etc.) of officers and employees of executive department.

Expenses and Supplies

[Note instruction 8]

Automobile service, including charges through clearing account 702.
Books and periodicals for office use.
House service. (See also account 707.)
Meals, including payments therefor on account of overtime work.
Membership fees and dues in associations.
Office supplies.
Postage.
Printing.
Repairs of furniture and office equipment and cost and repairs of individual items of small value or short life.
Stationery supplies.
Telephone and telegraph service, amounts paid others for.
Traveling expenses.

NOTE.—Membership fees and dues in assocations which do not have some direct or intimate relation to the telephone operations of the company shall be charged to account 323, "Miscellaneous income charges."

662. **Accounting department.**—This account shall include the pay, office, traveling and other expenses of officers, their assistants, and office forces, of the accounting department.

OFFICERS AND EMPLOYEES

[Note instruction 8]

Accountant. (See also note to this account.)
Addressograph clerks.
Auditor of disbursements.
Auditor of receipts.
Auditors—general and division.
Billing clerks.
Bookkeeper.
Chief accountant.
Chief statistician.
Chief traveling auditor.
Clerk.
Comptroller.
Division auditor of disbursements.
Division auditor of receipts.
General accountant.
Office manager. (See also note to this account.)
Plant accountant.
Revenue accountant.
Statistician.
Supervisors of methods, bookkeeping, vouchers, payrolls, estimates, etc.
Tax accountant.
Traveling auditor.
Vice president in charge of accounting department.
Assistants authorized to act for officers of accounting department.
Office and staff forces (e. g., staff assistants, secretaries, stenographers, messengers, office boys, etc.) of officers and employees of accounting department.

EXPENSES AND SUPPLIES

[Note instruction 8]

Automobile service, including charges through clearing account 702.
Books and periodicals for office use.
House service. (See also account 707.)
Meals, including payments therefor on account of overtime work.
Membership fees and dues in associations.
Office supplies.
Postage, including that used in mailing bills to customers by accounting department and in forwarding toll tickets to local collection offices.
Printing.
Repairs of furniture and office equipment and cost and repairs of individual items of small value or short life.
Stationery supplies.
Telephone and telegraph service, amounts paid others for.
Traveling expenses.

NOTE A.—The expense of accounting performed by employees of operating departments shall be charged to the appropriate accounts of those departments (e. g., the pay and expense of employees of local business offices engaged in keeping and billing customers' accounts shall be charged to account 645). (See also instruction 63.)

NOTE B.—Membership fees and dues in associations which do not have some direct or intimate relation to the telephone operations of the company shall be charged to account 323, "Miscellaneous income charges."

663. **Treasury department.**—This account shall include the pay, office, traveling, and other expenses of officers, their assistants and office forces, of the treasury department.

OFFICERS AND EMPLOYEES

[Note instruction 8]

Cashier. (See also note A to this account.)
Clerk.
Office manager.
Paymaster. (See also note A to this account.)
Supervisors of methods, stock and bond records, coupon payments, etc.
Stock and bond ledger clerks.
Treasurer.
Vice president in charge of treasury department.
Assistants authorized to act for officers of treasury department.
Office and staff forces (e. g., staff assistants, secretaries, stenographers, messengers, office boys, etc.) of officers and employees of treasury department.

EXPENSES AND SUPPLIES

[Note instruction 8]

Automobile service, including charges through clearing account 702.
Books and periodicals for office use.
House service. (See also account 707.)
Meals, including payments therefor on account of overtime work.
Membership fees and dues in associations.
Office supplies.
Postage.
Printing, including stock and bond certificates for transfer purposes. (See also note B to this account.)
Repairs of furniture and office equipment and cost and repairs of individual items of small value or short life.
Stationery supplies.
Telephone and telegraph services, amounts paid others for.
Traveling expenses.

NOTE A.—The pay and expenses of cashiers and paymasters employed by operating departments shall be charged to the appropriate accounts of those departments.

NOTE B.—The cost of printing stock certificates in connection with original and additional capital stock issues shall be charged to account 201. The cost of printing bonds in connection with new or additional issues of funded debt shall be accounted for as provided in instruction 15.

NOTE C.—Membership fees and dues in associations which do not have some direct or intimate relation to the telephone operations of the company shall be charged to account 323, "Miscellaneous income charges."

664. **Law department.**—This account shall include, when not provided for elsewhere, the pay, office and other expenses of officers, their assistants and office forces, and other employees of the law department, the cost of suits and other law costs, including law expenses connected with damages.

OFFICERS AND EMPLOYEES

[Note instruction 8]

Attorneys.
Claim agents, investigators, and adjusters. (See also note A to this account.)
Clerks.
Counsel.
General attorney.
General counsel.
General solicitor.
Law agent.

Law clerks.
Librarian.
Patent attorney.
Solicitor.
Special counsel.
Tax attorney.
Vice President in charge of law department.
Assistants authorized to act for officers of the law department.
Office and staff forces (e. g., staff assistants, secretaries, stenographers, messengers, office boys, etc.) of officers and employees of law department.

EXPENSES AND SUPPLIES

[Note instruction 8]

Automobile service, including charges through clearing account 702.
Agreements, briefs, contracts, legal forms and reports, cost of preparing and printing.
Collecting revenue and other accounts, law expenses in connection with.
Court expenses.
Depositions, cost of taking.
Examination of titles and other expenses incurred in suit to test validity of bond issue. (See also note B to this account.)
Fees and retainers of attorneys not regular employees.
Filing tax reports, passing tax claims, making returns to tax assessors, etc., cost of when handled by law department.
House service. (See also account 707.)
Law books and periodicals.
Law expenses in connection with rate cases or filing or adjustment of rate schedules
Law expenses of receivers.
Meals, including payments therefor on account of overtime work.
Membership fees and dues in associations.
Office supplies.
Postage.
Premiums on surety bonds.
Printing.
Repairs of furniture and office equipment and cost and repairs of individual items of small value or short life.
Special fees.
Stationery supplies.
Telephone and telegraph service, amounts paid others for.
Testimony, cost of printing and transcripts of.
Traveling expenses.
Witness fees.

NOTE A.—The pay and expenses of claim agents, investigators and adjusters employed by departments other than the law department shall be charged to the accounts of the department by which they are employed.

NOTE B.—Special law expenses incurred incident to the construction or purchase of telephone plant shall be charged to the appropriate telephone plant accounts; special law expenses incident to the issuance of funded debt shall be accounted for as provided in instruction 15.

NOTE C.—Membership fees and dues in associations which do not have some direct or intimate relation to the telephone operations of the company shall be charged to account 323, "Miscellaneous income charges."

665. **Other general office salaries and expenses.**—This account shall include the pay, office, traveling, and other expenses of officers, their assistants, and office forces of general offices not properly chargeable to other accounts, such as those engaged in editing magazines or periodicals published in behalf of all departments and employees engaged in detective or protective services for the company's interest as a whole.

EXPENSES AND SUPPLIES

[Note instruction 8]

House service. (See also account 707.)
Meals, including payments therefor on account of overtime work.
Office supplies.
Postage.
Printing, including cost of printing magazines or periodicals published in behalf of all departments.
Repairs of furniture and office equipment and cost and repairs of individual items of small value or short life.
Stationery.
Traveling expenses.

NOTE.—The expense of miscellaneous general activities when incidentally performed by employees of operating departments shall be included in the accounts of those departments. (See also instruction 63.)

V. OTHER OPERATING EXPENSES

668. **Insurance.**—(A) This account shall include the cost, not provided for elsewhere, of commercial insurance to protect the company against losses and damages in its telephone operations. (See also account 131.)

To this account shall be charged:

(1) The amount of insurance premiums paid to insurance companies.

(2) Special costs incurred in procuring insurance, such as brokerage fees, notarial fees, and insurance inspection service, and the pay, traveling, and office expenses of officers, clerks, and other employees of an insurance department.

(B) This account shall include also amounts credited to account 169, "Insurance reserve," for self-carried risks as provided in paragraph (B) of that account.

(C) This account shall include also the amount of insurance premiums covering blanket policies for which there is not available an equitable basis for allocation between the several accounts which may be involved.

(D) A list of representative losses and damages follows, the insurance premiums for protection against which are chargeable to this account when incurred in connection with the company's telephone operations:

LOSSES AND DAMAGES

[Note instruction 8]

Burglaries, holdups, check alterations, and forgeries.
Damages to the property of others.
Defalcations of employees and agents.
Fire and other casualties to telephone plant.
Fire and other casualties to telephone plant rented to others, the rents from which are includable in account 524.
Injury to or death of employees.
Injury to or death of persons other than employees.
Loss due to business interruption (i. e., use and occupancy insurance).

Loss of service of employees through death, sickness, injury, or other cause.
Loss of unbilled toll tickets.
Nonperformance of contractual obligations of others.

NOTE.—All losses and damages sustained, including those covered by commercial insurance or reserves carried in account 169 shall be charged to the depreciation reserve, telephone plant, repair, accident and damages, or other appropriate account, according to the character of the losses. Insurance recoverable or chargeable to account 169 on account of losses and damages sustained shall be credited to the account to which the losses and damages are chargeable.

669. **Accidents and damages.**—(A) This account shall include expenses, not provided for elsewhere, on account of persons killed or injured and property of others damaged in connection with the company's telephone operations.

(B) When an admitted liability arises because of an accident or damage, any portion of such liability, estimated if not known, chargeable to this account (i. e., the amount in excess of the liability insured) shall be charged hereto and credited to account 174, "Other deferred credits." When an estimated liability has been so charged to this account, appropriate adjustments between this account and account 174 shall be made when the extent of the liability has been definitely ascertained. (See also account 174 and instruction 4.)

(C) This account shall be credited and the appropriate property account charged with the amount of such accidents and damages due to construction work. (See also instruction 22–B–6.)

(D) Accident and damage payments provided for by commercial insurance or by a reserve for self-carried risks shall be credited to this account and charged to the insurer or to the reserve carried in account 169, "Insurance reserve," as appropriate.

ITEMS

[Note instruction 8]

Amounts paid in settlement of personal injury or damage claims.
Damage payments resulting from errors in directory listings, directory advertising errors and traffic service errors. (See also note A to this account.)
Damage to property of others, cost of. (See also note B to this account.)
Fees and expenses of surgeons, doctors, coroners, and undertakers.
Nursing, hospital attendance and medical and surgical supplies, cost of. (See also note C to this account.)

NOTE A.—Refunds of revenue overcharges in connection with such errors shall be charged to the revenue accounts originally credited.

NOTE B.—The cost of incidentally repairing property of others damaged in the course of maintenance or construction work shall be included in the cost of the work.

NOTE C.—Payments to or on behalf of employees, including accident and death benefits, salary, hospital attendance and medical supplies, also salaries, fees and expenses of surgeons, doctors, and nurses, etc., shall be charged to account 672 when coming within the scope of a company's general provision for employees' benefits.

NOTE D.—The pay and expenses of employees performing services in the investigation and adjustment of accident and damage claims shall be included in the accounts of the department by which such employees are employed.

671. **Operating rents.**—(A) This account shall include rents payable for the use of space in buildings occupied by the company,

space in conduits, pole line space for attachments, instruments, equipment, and other telephone plant, the rent for which is not provided for elsewhere.

(B) This account shall include also taxes borne by the lessee of property, the rent for which is chargeable to this account.

(C) This account shall include during each accounting period such portion of the book cost of leaseholds or similar interest in telephone property carried in account 211, "Land," as is necessary to cover the proportion of life thereof expired during such period. (See also account 172.)

ITEMS

[Note instruction 8]

Rents for location of poles, conduits, or cables.
Rents for use of general offices and central and branch telephone offices except rents chargeable to the clearing accounts.
Rents for use of ducts, conduits, and subways.
Rents for use of poles and buildings as supports for telephone circuits.
Rents for telephone instruments and equipment.
Rents for use of circuits.

NOTE A.—Expenses incurred by the company in maintaining and operating property, the rent for which is includable in this account, shall be charged to the operating expense account appropriate for owned property.

NOTE B.—This account shall not include rents provided for in the clearing accounts and in instruction 22-B-9.

NOTE C.—Rents for the exclusive use of telephone operating property held as a whole and operated by the company, such as a complete telephone plant, a complete exchange, or a complete toll system, shall be included in account 303.

672. **Relief and pensions.**—(A) This account shall include pensions or other benefits paid to active and retired employees, their representatives or beneficiaries, and salaries and expenses incurred in conducting relief, benefit, and general medical departments. It shall include payments to or on behalf of employees on account of injuries or accidental death when such payments come within the scope of a company's general provision for employees' benefits.

(B) If the company has definitely undertaken by contract to pay pensions to employees when regularly retired for superannuation or disability and has established a fund to be held in trust for such pension purposes, the company shall charge to this account monthly amounts determined through the application of equitable actuarial factors to the current pay rolls, which, together with interest accruals on the trust funds, will as nearly as may be, provide for the payment of such pensions, or for the purchase of annuities corresponding thereto. The amounts so charged shall be concurrently credited to a separate subaccount under account 170, "Provident reserve." The amounts accrued in each year shall correspond to the aggregate of the amounts expended directly by the company for pensions or annuities during the year and amounts paid into the trust fund. The company shall maintain a complete record of the actuarial computations through which the accrual each month of its pension liabilities is established.

(C) Upon the adoption of the accrual plan of accounting, pension payments to employees retired before the adoption of such plan shall be charged to an existing pension reserve or to account 413, "Miscellaneous debits to surplus." If a company pays into its pension trust fund the amount of its existing pension reserve, any such amounts in excess of provision for pensions granted prior to the adoption of the accrual plan may be applied in whole or in part to the adjustment of future accrual charges.

(D) Before adopting the accrual plan of accounting for pensions the company shall inform this Commission of the details of its pension plan giving full statement of the facts which in its judgment establish a contractual obligation for pension payments together with the actuarial formula under which it proposes to create its pension trust fund, and also a copy of the declaration of trust under which the fund is established.

(E) No charges to this account shall be made in anticipation of discretionary pension payments in the future.

(F) This account shall include also, under a separate subaccount, amounts accrued to provide for the payment of termination allowances or similar benefits to employees of the company when such employees are laid off because of lack of work and to provide necessary and warranted relief to former employees. Charges to this subaccount shall be made only after approval by this Commission of the company's plan for administering payments for these purposes and of the amount of the accruals. Amounts charged to this subaccount shall concurrently be credited to account 173, "Employment stabilization reserve."

ITEMS

[Note instruction 8]

Accident, sickness, death, and other disability benefits to employees, their representatives or beneficiaries.
Employees of relief, benefit, and general medical departments, pay and expenses of.
Expenses in connection with employees' disability cases, such as hospital, nursing, and medical attendance.
Fees and retainers for medical and similar services incurred by relief, benefit, and general medical departments.
House service. (See also account 707.)
Medical supplies.
Office supplies.
Postage, printing, and stationery.
Premiums paid for group insurance for the benefit of employees or their beneficiaries.
Repairs of furniture and equipment and cost and repairs of individual items of small value or short life.
Traveling expenses.

673. **Telephone franchise requirements.**—(A) This account shall include the cost not provided for in account 202, "Franchises," of all services, plant, materials and supplies, and similar items, including standard rates for telephone services, furnished to municipalities or other governmental authorities in compliance with

franchises, ordinances, or similar requirements and for which no reimbursement or payment is received by the company. (See also note A to this account.) It shall include the cost of paving and of premiums on bonds required under the general terms of a franchise or ordinance and not in connection with specific construction or maintenance work.

(B) This account shall be charged also each month with the amount necessary to cover such portions of the lives of limited franchises as have expired or been consumed during the month. Amounts so charged to this account shall be credited to account 172, "Amortization reserve," and shall be based upon such a rule as will accumulate by charges equitably distributed throughout the life of any franchise, a reserve that will at the expiration of the life of such franchise equal the original cost thereof.

(C) This account shall include also amounts paid for franchises running for one year or less after acquisition and may include direct charges for franchises acquired at small cost.

(D) Amounts charged to this account involving no direct money outlay, such as standard rates for telephone service rendered without charge, shall be credited to account 676, "Telephone franchise requirements—Cr."

NOTE A.—The cost of plant, supplies, etc., given as an initial consideration for a franchise running for more than one year shall be charged to account 202.

NOTE B.—Franchise taxes paid annually or more frequently shall be charged to account 305.

NOTE C.—The cost of plant used by a municipality without charge, or used by the company in rendering services to a municipality without charge, shall be included in the appropriate telephone plant accounts; maintenance expenses incurred in connection with such plant shall be charged to the appropriate maintenance accounts.

NOTE D.—The cost of reconstructing or changing the location of plant to conform with municipal requirements, including such work required under the provisions of a franchise or ordinance, shall be charged to the maintenance, telephone plant, and depreciation reserve accounts appropriate for the work performed.

674. **General services and licenses.**—This account shall include amounts payable for services received under a license agreement, a general service contract, or other arrangement providing for the furnishing of general accounting, engineering, financial, legal, patent, and other general services.

675. **Other expenses.**—(A) This account shall include all operating expenses not properly chargeable to other accounts.

(B) The cost of patents included in account 203, "Patent rights," shall be amortized by charging this account each month with the amount necessary to cover such portions of the lives of patents as have expired or been consumed during the month. Amounts so charged to this account shall be credited to account 172, "Amortization reserve."

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ITEMS

[Note instruction 8]

Amortization of patents, amounts paid for patents having an estimated service life of one year or less, patents acquired at small cost or in an undeveloped state and patents of doubtful service value.
Amounts paid incident to maintenance of associations of general character maintained on behalf of the company's telephone operations. (See also note A to this account.)
Commissions paid agents for leasing space to others in buildings partly occupied by the company in connection with its telephone operations.
Contributions for charitable or social or community welfare purposes which have a direct or intimate relation to the protection of the property of the company or to the development of its business or to the welfare of its employees.
Cost of publishing reports to stockholders, notices of stockholders' meetings, election of directors, conversion of bonds, and dividends declared.
Cost of valuations, inventories, and appraisals of telephone plant made for rate case purposes, and those taken in compliance with orders of Federal, State or other regulatory authorities. (See also notes B and C to this account.)
Fees and expenses of directors.
Fees of agents for registrations and transfers of outstanding capital stock.
Franks for use of officers and employees, cost of printing.
General audit of company's books by audit company, cost of.
House service furnished for space leased to others when not specifically reimbursed.
Losses from foreign exchange. (See also instruction 7.)
Loss of current funds due to bank failures.

NOTE A.—Salaries and expenses of employees representing the company in associations of a general character maintained by the company in connection with its telephone operations shall be included in the accounts chargeable with the cost of the regular activities of such employees. Salaries and expenses of employees engaged in work in connection with employees' associations shall be included in the appropriate departmental accounts.

NOTE B.—The cost of valuations, inventories and appraisals taken in connection with the contemplated purchase or sale of property shall be charged to account 139 pending further disposition.

NOTE C.—The pay and expenses of officers and employees performing incidental services in valuations, inventories and appraisals shall be included in the accounts ordinarily charged with their pay and expenses. (See also instruction 63.)

NOTE D.—Contributions for charitable or social or community welfare purposes which do not have a direct or intimate relation to the protection of the property of the company or to the development of its business or to the welfare of its employees shall be charged to account 413, "Miscellaneous debits to surplus."

676. **Telephone franchise requirements—Cr.**—This account shall be credited with amounts included in account 673, "Telephone franchise requirements," for which there is no direct money outlay, such as standard rates for telephone service furnished without charge to municipalities in accordance with franchise requirements.

677. **Expenses charged construction—Cr.**—This account shall be credited and the appropriate construction accounts charged with amounts, not provided for elsewhere, representing the portion of operating expenses applicable to construction work. (See also instruction 22–B–1.)

CLEARING ACCOUNTS

(Note particularly instructions 2–C and 70)

702. Vehicle and other work equipment expense.
704. Supply expense.
705. Engineering expense.
706. Plant supervision expense.
707. House service expense.

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702. Vehicle and other work equipment expense.—(A) This account shall include the expense of operating vehicles and other work equipment, including the expenses of garages, shops, tool rooms, and stables and the amount of depreciation charges applicable to the accounting period for plant classified in account 264, "Vehicles and other work equipment."

(B) This account shall be cleared by adding to the cost of work performed such amounts as will distribute such expense equitably.

ITEMS

[Note instruction 8]

Books and periodicals.
Depreciation of vehicles and other work equipment.
House service. (See also account 707.)
Insurance (see also note to account 668), including that against losses and damages to or by vehicles and other work equipment.
License fees for vehicles and for drivers.
Office supplies.
Overages and shortages in material and supplies for vehicles and other work equipment.
Postage, printing, and stationery.
Rent paid for and repairs of rented vehicles and other work equipment, garages, shops, tool rooms, stables, and other quarters. (See also instruction 23.)
Repairs of furniture and office equipment and cost and repairs of individual items of small value or short life.
Repairs of vehicles and other work equipment and cost and repairs of individual items of small value or short life.
Supplies, such as feed, fuel, gasoline, oil, tires, tubes, tire chains, soap, waste, sponges, measures, funnels, electric power, etc., used in the operation of vehicles and other work equipment, garages, shops, tool rooms, and stables.
Supervising officers, and their office and field forces, including inspectors, testers, garage men, and other employees, pay and expenses of.

704. Supply expense.—(A) This account shall include the expenses incurred in connection with the purchase, storage, handling, and distribution of material and supplies which are not allocated to other accounts as incurred.

(B) This account shall be cleared by adding to the cost of material and supplies a suitable loading charge which will distribute the total expense equitably.

ITEMS

[Note instruction 8]

Books and periodicals.
Discounts on material, cash and other. (See also note A to this account.)
House service. (See also account 707.)
Overages and shortages in material and supplies which can not be assigned to specific accounts. (See also accounts 122 and 702.)
Insurance (see also note to account 668) including that against losses and damages to material and supply stock.
Losses due to depreciation, breakage, leakage, evaporation, and fire and other casualties to supply stock not assigned to specific accounts nor distributed through the pricing of materials and supplies disbursed.
Office supplies.
Postage, printing, and stationery.
Purchasing agents, superintendents and supervisors of supplies, managers of stores, storekeepers, clerks, and laborers, pay and expenses of.
Rent paid for and repairs of rented storehouses, storerooms, storage yards, and other quarters. (See also instruction 23.)
Repairs of furniture and office equipment and cost and repairs of individual items of small value or short life.
Transportation charges, undistributed. (See also note B to this account.)
Traveling expenses.

NOTE A.—So far as practicable, cash and other discounts on material shall be deducted in determining the cost of the particular material to which they relate or credited to the account to which the material is charged.

NOTE B.—Transportation charges on material purchased shall be so far as practicable included as a part of the cost of the particular material to which they relate. Transportation charges on material recovered from plant shall be charged to the account to which the cost of removal is charged.

705. **Engineering expense.**—(A) This account shall include the expenses of the general engineering department.

(B) This account shall be cleared by apportioning the total expenses to the appropriate accounts on the basis of service rendered, as deterimned by the time devoted to particular jobs or on such equitable basis as may be fixed by the officers of the company.

ITEMS

[Note instruction 8]

Books and periodicals.
Engineering officials and employees, pay and expenses of.
House service. (See also account 707.)
Office supplies.
Postage, printing, and stationery.
Rent paid for and repairs of rented offices. (See also instruction 23.)
Repairs of furniture and office equipment and cost and repairs of individual items of small value or short life.
Tools and instruments of small value or short life.
Traveling expenses.

706. **Plant supervision expense.**—(A) This account shall include the expense of general supervision of the maintenance and construction of the plant where a department of the company's organization is charged with both maintenance and construction.

(B) This account shall be cleared on the basis of labor supervised except that charges for plant engineering shall be cleared by apportioning such expense to the appropriate accounts on the basis of the

time devoted to particular jobs or on such equitable basis as may be fixed by the officers of the company.

ITEMS

[Note instruction 8]

Books and periodicals.
House service. (See also account 707.)
Office supplies.
Plant supervising officers and their staffs, including engineers, office and field forces charged with planning for and superintending the work of maintenance and plant construction, pay and expenses of. (See also note to this account.)
Postage, printing, and stationery.
Rent paid for and repairs of rented offices. (See also instruction 23.)
Repairs of furniture and office equipment and cost and repairs of individual items of small value or short life.
Traveling expenses.

NOTE.—The pay and expenses of foremen in direct charge of jobs, general foremen and other supervisory employees not engaged in the general supervision of maintenance and construction work, such as local plant administrative employees whose duties are limited as to functions or areas, shall be included in the cost of the work supervised and not charged to this account.

707. **House service expense.**—(A) This account shall include the expenses of operating offices and buildings, whether owned or rented, when such expenses are not allocated, as they are incurred, to the operating expense and other accounts.

(B) This account shall be cleared by apportioning the entire expense to the operating expense and other accounts on the basis of the use made of such property.

ITEMS

[Note instruction 8]

Building superintendents and others engaged in supervising house service operations, pay and expenses of.
Cleaning supplies.
Elevator service.
Fuel.
Heat.
Ice.
Janitor service.
Light.
Office supplies.
Postage, printing, and stationery.
Power. (See also accounts 604 and 610.).
Rent paid for and repairs of rented quarters used in the supervision of general house service operations, other than space used by janitors and similar employees in furnishing house service for a particular building. (See also instruction 23.)
Repairs of furniture and office equipment and cost and repairs of individual items of small value or short life.

APPENDIX A

UNITS OF PROPERTY

The following list of units of property shall be used in connection with the accounting provided in instructions 24 and 25 but shall not be considered as determining the classification of the telephone plant involved.

212. **Buildings.**

A complete building.

An entire roof with or without supporting members.

NOTE A.—A building of irregular shape having more than one roof level may have several isolated roofs, each of which shall be considered an entire roof. In the case of buildings to which lateral extensions have been made, even though having but one roof level, that part of the roof covering an entire section built at one time shall be considered an entire roof.

A complete fire escape.

A complete metal window (i. e., box, frame, and sash).

A boiler, furnace, hot water heater, or automatic stoker.

A coal or ash conveying system.

An elevator complete with operating mechanism.

A gas-burner system.

A house-lighting or power board.

An oil-burner system.

An oil tank.

The floor covering for one room.

A motor, generator, engine, turbine, pump, compressor, ventilating fan, air washer, elevator drum, or similar item of equipment, with or without associated wiring, control equipment, etc.

NOTE B.—In addition to the above units of property, material (i. e., portions of buildings, equipment, fixtures, etc.) installed and retired, and the labor and incidental costs involved in connection with work of the following character, shall be handled through the telephone plant and depreciation reserve accounts.

(1) Changes in the type of operation of elevator systems, e. g., a change from manual to signal control of cars, from manual to power operation of doors, from low speed to high speed, from direct to alternating current, from hydraulic to electric operation, from one type of signaling or dispatching system to another.

(2) Relocations of toilet rooms, battery rooms, kitchens, terminal rooms, machine rooms, transformer-vaults, etc.

(3) Structural changes such as: (*a*) Reinforcements of floors, roofs, bearing walls, footings, and foundations; (*b*) additions or relocations of elevator shafts stairways, fire exits, and vaults, but excluding switchboard ca[illegible] holes and slots; and (*c*) building alterations required for fire protectio[illegible]nd other safety measures.

(4) Changes in the type of electric current supply, or of ventilating, air conditioning, or similar systems.

(5) Building enlargements.

(6) Replacements of the following character—

(*a*) Replacements of plumbing or heating pipes (with or without associated valves) except when necessitated by minor repairs or minor relocations of fixtures.

(*b*) Replacements of all or substantially all of the lighting fixtures (with or without associated wiring and conduit) in one operating or equipment room or, in the case of office space, on one floor of a building.

(*c*) General replacements (throughout a building or throughout an entire portion erected at one time) of items such as supply, return, or air valves in heating systems; hot or cold water valves or faucets; plumbing, heating, or drainage traps.

221. **Central office equipment.**

Switchboards, desks, and testboards—

Switchboards (i. e., local, toll, dial system "A," cordless "B," call distributing "B," observing, teletypewriter, etc.)—A complete section or lower unit.

Desks (i. e., operating, observing, testing, etc.)—A complete section.

Testboards, or test and control boards (board type)—A complete section.

Testboards, or test and control boards (rack type)—

All the equipment in one bay.

A complete upper unit.

A complete lower unit.

A complete installation of rack framework for one board.

Test panels—A complete panel.

Test cabinets—A cabinet complete with equipment.

Distributing frames—

Main distributing frames (including wall type)—A complete installation for one central office (in multi-unit offices, for one operating unit).

Intermediate distributing frames—A complete installation for one central office (in multi-unit offices, for one operating unit).

Mezzanine balconies—A complete installation for one frame.

Racks—

Relay rack equipment—

A panel or unit complete with equipment.

All the equipment in one bay, exclusive of any panels or units.

Coil rack equipment—All the equipment on one shelf.

Message and traffic register rack equipment—All the equipment in one bay.

Iron framework—A complete line of rack with or without inclosing cabinet or case.

221. **Central office equipment**—Continued.

Cable—

All of the cables in one run used for the same purpose, such as between—

(1) Main frame and intermediate frame for subscribers' lines.

(2) Main frame and intermediate frame for outgoing trunk multiple.

(3) Intermediate frame and connector frame or final frame for subscribers' lines.

(4) Intermediate frame and answering jacks.

(5) Intermediate frame and switchboard for outgoing trunk multiple jacks.

(6) Intermediate frame and switchboard for subscribers' multiple jacks.

Iron framework—A complete installation of rack for one cable run.

Power equipment—

Frame or rack mounted equipment—

A panel or shelf complete with equipment, such as fuses, meters, control equipment, etc.

Iron framework—A complete line of frame or rack for one fuse board, one power switchboard, etc.

A generator, motor, motor-generator set, gas engine, rectifier, ringing machine, harmonic converter, pole changer, interrupter, power filter, or choke coil.

Storage batteries:

A complete battery with or without rack, cabinet, or counter electric motive force cells.

All positive or all negative plates in an entire battery (i. e., in all cells of a 24-volt battery, in all cells of a Morse battery, etc.).

All tanks or all jars of an entire battery.

A complete battery rack or cabinet, storage or dry.

A complete group of bus bars, cable, or wiring (with or without conduit) such as between—

Battery and fuse panel.

Power switchboard and machines.

Telephone repeater equipment (including testing equipment)—

A complete floor mounted rack type set.

Relay rack mounted equipment—

A panel or unit complete with equipment.

All the equipment in one bay, exclusive of any panels of units.

Coil rack mounted equipment—All the equipment on one shelf.

Iron framework—A complete line of rack.

221. Central office equipment—Continued.

Carrier equipment (telephone, telegraph, repeater, and testing equipment)—

A complete floor mounted rack type set.

Relay rack mounted equipment—

A panel or unit complete with equipment.

All the equipment in one bay, exclusive of any panels or units.

A line filter.

A complete test table.

Iron framework—A complete line of rack.

Telegraph equipment (printer and manual)—

Telegraph testboards—A complete section or bay.

Duplex, single line telegraph, and polar repeaters—A table or bay complete with equipment.

Metallic telegraph repeaters—

A complete floor mounted rack type set.

A panel or unit complete with equipment.

Voice frequency carrier equipment—A panel or unit complete with equipment.

Voice frequency carrier battery supply apparatus—

A complete bay of equipment.

A complete test table.

Iron framework—A complete line of rack.

Telephotograph equipment—

Table-mounted sending or receiving equipment—

A table complete with equipment.

A complete optical system.

A complete mechanical system.

A complete fork box.

A complete amplifier-modulator box.

Rack-mounted sending or receiving equipment—

A panel complete with equipment.

All the equipment in one bay.

Iron framework—A complete line of rack.

Power equipment—

A complete power board.

A complete storage battery.

Photographic equipment—

A copying camera or a copying, enlarging, and reducing camera, each with or without associated stands, illuminators, and copy boards.

A print machine.

A drying cabinet.

A developing, fixing, and washing tank.

Radio equipment—

A complete transmitter.

221. Central office equipment—Continued.

Miscellaneous equipment—

A calculagraph, a master clock, or a secondary clock.

Electrically driven calculagraph and clock systems—A complete installation.

Mechanical or pneumatic tube ticket distributing system—A complete installation.

Each complete tool or portable test set the original cost of which was charged to the telephone plant account, such as a plug remover and attacher, cam aligning fixture, multiple bank resetting gauge, or shaft straightening tool, a relay adjusting set, line finder set, or wagon type set.

Each complete item of furniture or other miscellaneous equipment, the original cost of which was charged to the telephone plant account, such as a desk or table equipped with central-office equipment, an operator's chair, a complete switchboard platform, an operator's telephone set cabinet, a rotary file or directory cabinet, a ticket cabinet or rack, a tarpaulin with or without cabinet, a portable service-observing cabinet, or a holding-time recorder.

Loud-speaker equipment—A complete installation.

Aisle-lighting equipment—A complete installation on one floor.

Rolling ladders—A complete installation for one side of one frame or rack.

Message and traffic register cabinets—A cabinet complete with equipment.

Teletypewriter sets—Units specified under account 231.

Panel dial system equipment—

A complete equipment frame such as line-finder frame, line-switch frame, selector frame, link frame, routine test frame, decoder frame, sender frame or floor alarm board.

Pulse-machine equipment—A complete pulse machine.

Pulse-machine control apparatus—A complete installation controlling a set of pulse machines.

Step-by-step dial system equipment.

A complete equipment frame, such as a line-finder frame, line-switch frame, selector frame, connector frame, or repeater frame.

Key-indicator equipment or key-pulsing equipment.

A complete equipment frame, such as a link or sender frame.

NOTE.—When work of the following character is performed as a special job in a central office or at a multiple or dial private branch exchange for the purpose of improving or changing the type of the equipment, the material installed and retired and the labor and incidental costs involved shall be handled through the telephone plant and depreciation reserve accounts.

(1) Conversions of one or more switchboard positions, or dial-system frames, from one type to another, such as from subscribers' to toll, subscribers' to rural, inward toll to combined line and recording, manual B to call indicator B, or from panel B switchboard incoming frame to interoffice incoming frame.

(2) Conversions of circuits from one type to another, such as conversions of cord circuits from two-party ringing to four-party selective ringing, semiselective ringing to selective ringing, or from manual recall to flashing recall, and conversions of panel-sender circuits from noncoin to coin and from two digit to three digit.

(3) Replacements of items of one type, with items of a different type for such reasons as improving signaling or transmission characteristics, changing operating methods or increasing the capacity of the office, e. g.:

(*a*) Replacements of all the relays or repeating coils of one type in a central office with relays or coils of an improved type for the purpose of improving the signaling or transmission characteristics.

(*b*) Replacements of items of equipment in dial offices because of a change in the method of operation to multiple registration.

(*c*) Replacements of items of power equipment because of a change in power purchased from direct current to alternating current.

(*d*) Modifications of the trunk and cord circuits of multiple manual private branch exchange boards necessitated by a cutover of a central office district to dial operation.

(*e*) Replacements of protectors of one size with protectors of a smaller size on a main distributing frame so that more protectors may be installed in the same space.

(*f*) Replacements of 20 pair terminal strips on a main distributing frame with 50 pair strips to increase the capacity of the frame.

(*g*) Replacement of jack strips having 10 jacks per strip with strips having 20 jacks per strip to increase the capacity of a switchboard.

(*h*) Replacement of keys of one type with keys of a different type to permit more keys to be placed in the same position.

231. **Station apparatus.**

A complete station.
A desk stand, with or without transmitter, receiver or dial.
A hand set (i. e., transmitter, receiver and handle).
A hand set mounting, with or without dial.
A wall set with or without transmitter, receiver or dial.
A bell box or other subscriber set, such as extension bell, signal horn, etc.
A coin collector with or without transmitter, receiver or dial.
A complete apparatus cabinet.
A complete key cabinet or key box.
An intercommunicating system key.

NOTE.—The cost less salvage of the following items of station apparatus not designated units of property shall be charged to the depreciation reserve account when lost, destroyed, junked, or otherwise disposed of:

A hand set handle.
A transmitter.
A receiver.
A dial.
A dial mounting.
A switching key (individually mounted type).

231. **Station apparatus**—Continued.

Teletypewriter equipment—

A complete station.
A printer or teletypewriter.
A printer or teletypewriter table or stand.
A base (printer or reperforator).
A cover (printer or reperforator).
A printer unit or typing unit.
A keyboard unit.
A distributor unit.
A transmitter unit.
A perforator unit.
A reperforator unit.
A relay box with equipment.
A motor or motor unit (excluding the motor of a motor generator set).
A motor generator set.
A rectifier unit.
A loop switchboard.
A station signaling set.

Manual telegraph equipment—

A complete station.
A loop switchboard.

Program supply and public address equipment—

A microphone transmitter.
A microphone transmitter mounting.
An amplifier.
A loud speaking receiver.
A horn.
An observer's telephone set.
A complete dynamotor, motor-generator, rectifier or storage battery.
A complete control cabinet, resistor cabinet or junction box.
A battery cabinet.
Rack mounted equipment:
All the equipment in one bay.
A panel complete with equipment.
Iron framework—A complete line of rack.
Portable equipment—A complete item of portable equipment, with or without the carrying case (e. g., an amplifier, a transmitter mixing panel, an oscillator or an equalizer).
Radio receiving sets and equipment associated therewith—A complete installation.

232. **Station installations.** (See instruction 25, par. B.)

233. **Drop and block wires.** (See instruction 25, par. B and account 605, "Repairs of station equipment.")

234. **Private branch exchanges.**

A complete cordless or nonmultiple switchboard, with or without local storage batteries or cables classified as P. B. X. equipment.

An apparatus cabinet as used with certain nonmultiple boards.

A complete section of an order receiving table.

An order turret (not including the turrets forming part of an order receiving table).

An attendant's cabinet complete with equipment.

A code sending set or code call unit.

A complete teletype switchboard.

An operator's chair.

Multiple private branch exchange equipment and private dial system equipment (except as provided below)—Units specified under account 221.

An equipment cabinet complete with batteries and switching equipment mounted therein, as generally used with a dial system installation of small capacity.

Local storage battery plants of the type used to serve several nonmultiple boards or of the type used with certain small multiple P. B. X. installations—An entire battery with or without cabinet or control apparatus.

Local automatic power plants of the type used to serve a small dial or a small multiple P. B. X.—

A control cabinet, with or without charging or ringing equipment.

An entire battery, with or without cabinet or counter E. M. F. cells.

235. **Booths and special fittings.**

A booth compartment with or without special fittings or associated furniture and fixtures such as chairs, directory racks, directory tables, and counters.

An attendant's desk including equipment or a switchboard.

241. **Pole lines.**

A pole (i. e., line pole, brace pole, guy stub, or pole forming part of A or H fixture), a pole stub, or a pole butt with or without associated anchors, guys, steps, etc.

A crossarm (i. e., wooden crossarm, guard arm, or cable crossarm, including extension arms) with or without associated braces and other hardware.

A special fixture (i. e., a bridge fixture, a tower or other special-river crossing or long-span fixture) with or without associated anchors, guys, etc.

242. Cable.

A span of cable with or without associated suspension strand, clamps, rings, etc. (The term "a span" shall include a length of cable from a "Y" splice not located at a pole to a pole or building.)

A section or run of cable with or without associated elements and parts as follows:

(1) Between a manhole, handhole, or service box and a pole, building, fence, wall, or the junction with house cable.

(2) Between manholes, handholes, or service boxes; or between an office cable vault and an office manhole.

(3) Between a cable vault or an office manhole and the junction with the main frame terminating cables.

(4) A section of buried cable 300 feet or more in length, or a section of buried cable between manholes, splicing boxes, or pedestals.

(5) All of a continuous run of one size of house cable. ("All of a continuous run of one size" means a section between splices other than straight splices.)

(6) All of a continuous run of one size of block cable, i. e., cable attached to buildings, walls, or fences. ("All of a continuous run of one size" means a section between splices other than straight splices.)

(7) All of a submarine cable for one crossing; or a section of submarine cable 300 feet or more in length.

(8) A section of underground dip cable between poles and/or buildings, or the appropriate units listed above.

Any length of cable which is a continuation of a unit of cable and is replaced with such unit.

Any length of cable connected with but not a part of a terminal or a case of equipment such as loading coils when replaced with the terminal or case of equipment.

Main frame terminating cables (generally silk and cotton insulated)—All the cables including forms used for terminating one outside cable.

A complete cable terminal, protected or unprotected, with or without associated balcony, pole seat, pedestal, etc.

A pressure contactor terminal with or without contactor.

A house cable terminating frame.

A submarine cable hut or house.

A submarine cable anchorage.

A submarine cable terminating frame.

A fuse pot.

A case of equipment such as loading coils, building-out condensers, carrier line filters, or auto-transformers.

243. Aerial wire.

Two continuous spans or more of one wire with or without associated insulators, transposition brackets, etc.

A case of equipment such as loading coils, building-out condensers, carrier line filters, or auto-transformers.

An antenna, complete with or without supports.

244. Underground conduit.

A section of conduit—

(1) Between two manholes, handholes, or service boxes.

(2) Between a manhole, handhole, or service box and a pole or building.

(3) Between a central-office cable vault and an office manhole.

(4) Underground dips—between two poles; between a pole and a building; between two buildings; or units (1) and (2) above.

A manhole, handhole, or service box.

NOTE.—When a manhole is reconstructed, i. e., enlarged or changed in design, the investment representing portions of the manhole removed, whether or not replaced, should be written off to the depreciation reserve account.

261. Furniture and office equipment.

Each complete item of furniture or equipment, the original cost of which was charged to the telephone plant account, such as—

A desk, chair, table, piano, davenport, typewriter, computing machine; a section of bookcase, filing cabinet, shelving, bins, or counter; a rug, a carpet, or other floor covering for one room.

264. Vehicles and other work equipment.

Each complete item of equipment, the original cost of which was charged to the telephone plant account, such as—

A passenger automobile or truck with or without body; a tractor; a pole jack, splicer's tent or extension ladder; a pole derrick, power winch, earth boring machine, or trailer; a portable test set; a wire measuring machine.

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[fol. 577] [Title omitted]

AFFIDAVIT OF HAROLD V. BOZELL ON BEHALF OF ADDITIONAL PLAINTIFFS IN SUPPORT OF MOTION FOR INTERLOCUTORY INJUNCTION

UNITED STATES OF AMERICA,
Southern District of New York,
County and State of New York, ss:

Harold V. Bozell, being duly sworn, deposes and says:

1. He is Executive Vice President of General Telephone [fol. 578] Service Corporation; said Corporation has a contract with each of Indiana Associated Telephone Corporation, Interstate Telephone Company, Michigan Associated Telephone Company, Ohio Associated Telephone Company, Pennsylvania Telephone Corporation, Southwestern Associated Telephone Company and Tri-State Associated Telephone Corporation, pursuant to which said General Telephone Service Corporation, through its officers, assists said corporations in the operation of their business and the keeping of their books, records and accounts relating thereto; and as such Executive Vice President of said General Telephone Service Corporation he is, therefore, thoroughly familiar with the business and the books, records and accounts of all of said corporations above named.

2. The requirements of the Uniform System of Accounts for Telephone Companies prescribed by the Federal Communications Commission by Order No. 7-C are arbitrary, unfair, unreasonable and confiscatory in respect to all said above named corporations and will result, if complied with by said corporations, in substantial injury to said corporations and their stockholders, bondholders and rate payers. Compliance with the requirements of said Uniform System of Accounts would result in the statements of the financial conditions of said corporations presenting an unfair and inaccurate description of the assets and earnings of said corporations and would subject them to burdensome and unnecessary expenses.

3. By such System of Accounts said corporations would be required to separate their investment in property used

and useful in the telephone business into four separate accounts, namely, "Telephone plant in service," (Account 100.1); "Telephone plant under construction," (Account 100.2); "Property held for future telephone use," (Account 100.3); and "Telephone plant acquisition adjust-
[fol. 579] ment," (Account 100.4). The System of Accounts permits to be included in the "Telephone plant in service" account only the "original cost" of the telephone plant used in the telephone service by the accounting corporation and such original cost is defined as, not the cost to the accounting company, but "the actual money cost of — property at the time when it was first dedicated to the public use, *whether by the accounting company or by a predecessor public utility.*" The balance of the cost to the accounting company of its investment in telephone property used in telephone service must be entered in Account 100.4, "Telephone plant acquisition adjustment account."

4. This separation into two separate accounts, of the accounting companies' investments fairly made in property used and useful in the telephone business, by itself, will result in irreparable damage to the above named corporations. The separation of this investment into the two accounts, together with the name of the accounts, namely, "Telephone plant in service" and "Telephone plant acquisition adjustment," will necessarily result in creating the unfair and damaging understanding in stockholders, bondholders, prospective investors, regulatory bodies and rate payers that the account entitled, "Telephone plant in service" is the fair measure of the investment on property used and useful in the telephone business, in spite of the fact that the amount of such account will, in the case of the above named corporations, be entirely arbitrary and inaccurate and will have no relation whatsoever to the investment of said corporations in said property or to the value thereof. Furthermore, it is apparent from the name of Account 100.4, namely, "Telephone plant acquisition adjustment," that it is the intention and belief of the Federal Communications Commission that the amount contained in such account should not properly be continued on the books of said corporation as an asset, but should disappear from [fol. 580] said books and from the records of said corporation. This interpretation of the purpose of the segregation in the said two accounts is confirmed by the provisions of

instruction 100.4C, which provides with respect to said "Telephone plant acquisition adjustment" account that, "the amounts recorded in this account with respect to each property acquisition shall be disposed of, written off, or provision shall be made for the amortization thereof in such manner as this Commission may direct."

5. The only apparent purpose served by the segregation required by said Uniform System of Accounts is to make the balance sheets of telephone companies required to comply therewith the basis for the application of a specific rate-making formula, which is contrary to the decisions of the Supreme Court with respect to the rights of operating public utility companies to a fair return upon the fair value of their property devoted to the public use. The continuous maintenance, moreover, of such separate accounts will burden, arbitrarily and unnecessarily, such companies with heavy expenses. To the extent that information as to original cost, as defined in the Uniform System of Accounts, is available or can be provided in the manner desired by the Federal Communications Commission, it can be provided in supplementary statements, which said corporations have formally offered to provide to the Commission, and this information can be furnished without the expense of continuously maintaining the separate and arbitrary accounts on the books, without making misleading, the balance sheets and operating statements of the corporations and without destroying or prohibiting the keeping of records of the accounting companies descriptive of their own financial transactions.

6. The segregation of the investment of the above named corporations into said two accounts will be, because of the history and development of the telephone properties owned by them, particularly and entirely misleading, inaccurate and arbitrary. The telephone businesses owned by each of said corporations are aggregations of local exchanges, [fol. 581] most of them in small communities in the several states in which they operate, practically all of which exchanges were owned and were built in the first instance by separate corporations or mutual organizations. All but 2 of the approximately 669 communities served, have but a single telephone exchange. The records now available indicate that the said seven telephone companies had at least 233 predecessors. The records of the immediate predeces-

sors were, in almost every case, inadequately and inaccurately kept and were themselves in turn based upon purchases of going businesses from other telephone companies. In many instances no records at all were kept by the companies who originally "dedicated to the public use" the telephone plant now owned by such seven corporations and in many other cases the books and records of the companies dedicating such plant to the public use are not now available to the owning corporation, or, if available, are known to be inaccurate.

It is estimated that it would be impossible either to determine or to estimate, with any satisfactory degree of accuracy, the original cost of more than one-half of the property now owned by said corporation. The greater part of the properties purchased by the said corporations has been recorded at the actual cost thereof, either in cash or securities, to the purchasing corporation. The entirely false and erroneous impression that will be given by this segregation as to each of the above named corporations will more fully appear from the statement of important facts with respect to such companies given below.

7. Said Uniform System of Accounts appear to permit charges against earnings to provide a reserve for depreciation only with respect to property included in Account 100.1, "Telephone plant in service." The amount in this account, in the case of the above named corporations, would be but a part of their prudent investment in depreciable property used and useful in the telephone business. For [fol. 582] the purpose of maintaining intact their investments in such property used and useful in the telephone business and the investment of their security holders, said corporations have adopted and followed the policy of making monthly charges to income to provide against depreciation of the property owned by them, such charges being made in such amount as the respective Boards of Directors determine from time to time to be necessary, in view of all the circumstances, to provide a sufficient reserve against depreciation of all the depreciable property of said corporations used and useful in the telephone business, so that their investment in such property may be kept intact and safe. Such protection of said investment is not only their right but also their duty. If the corporations are allowed to make provision for depreciation only on the basis of

the amount permitted to be recorded in the "Telephone plant in service" account, it will be impossible for them to build up adequate reserves against the actual depreciation suffered by their property. Adequate provision for depreciation is essential to the protection of their security holders and of their customers.

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[fol. 583] 10. Instruction B-1 of said Uniform System of Accounts provides: "All charges to the accounts prescribed in this classification for telephone plant, income, operating revenues, and operating expenses shall be just and reasonable and any payments by the company in excess of such just and reasonable charges, shall be included in Account 323, 'miscellaneous income charges.'" Since the burden of sustaining every accounting entry is on the company, it is evident from this provision that the Federal Communications Commission intends to substitute its judgment as to what is just and reasonable for the judgment of the management and to order charges to Account 323 of any differences between what the companies have actually spent and recorded and the amounts which the Commission decides to be just and reasonable. No such power has been or could be vested in the Commission by Congress. Such a power in the Commission would constitute an unlawful interference with management; and would subject the accuracy of all operating statements to doubt, as this power would result in the Commission censoring expenditures of a company after they have been made and recorded, thus making actual changes in earnings statements, which may already in good faith have been published to the stockholders and the public as being the actual history or record of operations of a company. The jurisdiction of the Com-[fol. 584] mission may extend to judging in formal rate cases as to the reasonableness of expenditures, but certainly not to the modifying of records of actual expense to reflect the Commission's judgment of what the expense should have been, rather than what it actually was.

11. Following is a statement of some of the important facts relating to the organization and acquisition and description of the properties owned by the above named corporations:

Indiana Associated Telephone Corporation

Indiana Associated Telephone Corporation (hereinafter called "Indiana") was incorporated under the laws of the State of Indiana in 1930. It owns and operates within the State of Indiana 27 local exchanges in at least 27 communities within said State, serving approximately 35,000 stations. All of said exchanges were acquired by said Indiana by purchase in 1932, with the approval of the Indiana Public Service Commission and the fixed properties purchased were recorded at the cost to it in securities issued therefor.

The exchanges now owned by Indiana were acquired through a series of successive purchases by it and its numerous predecessor companies. By a similar series of purchases by Indiana and its various predecessor companies, Indiana acquired and now owns telephone lines in numerous rural communities built by farmers' mutual associations and connected with the exchanges now owned by Indiana. The records of Indiana indicate that at least 22 separate known corporations or other organizations have owned some part of the properties now owned by it; that of such 22 predecessors the records of all thereof are either totally lacking or are known to be inadequate for the purpose of determining the original cost of the property acquired by Indiana at the time of the dedication thereof to the public service; and it is estimated that the original cost of substantially all of the property purchased by Indiana cannot be determined by it or even estimated with any satisfactory degree of accuracy. It is impossible to segregate [fol. 585] property purchased by Indiana from property constructed by it since 1932, but it still represents a very substantial portion of all the fixed property now owned, which, as of October 31, 1935, was recorded at $6,851,893.46.

Interstate Telephone Company

Interstate Telephone Company (hereinafter called "Interstate") was incorporated under the laws of the State of Idaho in 1930. It owns and operates within the States of Idaho, Washington and Montana 42 local exchanges in at least that number of communities within said States, serving approximately 18,765 stations. All of said exchanges were acquired by said Interstate by purchase as of or subsequent to January 1, 1931. These purchases were

recorded at actual cost to Interstate, either in cash or securities, and property additions of approximately $875,000., constructed subsequent to said date, have been recorded at cost. The fixed property of Interstate recorded on its books as of October 31, 1935 was $4,684,262.29.

The exchanges now owned by Interstate were acquired through a series of successive purchases by it and its numerous predecessor companies. By a similar series of purchases by Interstate and its various predecessor companies, Interstate acquired and now owns telephone lines in numerous rural communities built by farmers' mutual associations and connected with the exchanges now owned by Interstate. The records of Interstate indicate that more than 22 separate known corporations or organizations have owned some part of the properties now owned by it; that of such 22 known predecessors the records of all are either totally lacking or are known to be inadequate for the purpose of determining the original cost of the property purchased by Interstate at the time of the dedication thereof to the public service; and that the original cost of at least 80 per cent. of the book value of the property now owned by Interstate cannot be determined or estimated by it with any satisfactory degree of accuracy.

[fol. 586] Michigan Associated Telephone Company

Michigan Associated Telephone Company (hereinafter called "Michigan") was incorporated under the laws of the State of Michigan as Michigan Home Telephone Company in 1926. It operates in the State of Michigan some 69 local exchanges in at least 69 communities within said State, serving approximately 31,204 telephone stations. All of said exchanges were acquired by said Michigan by purchase.

The purchases of said exchanges were all authorized by the Public Utilities Commission of the State of Michigan, and substantially all the properties are recorded on the books of Michigan at the prices paid therefor in accordance with the authority of said Commission.

The exchanges now owned by Michigan were acquired through a series of successive purchases by it and its numerous predecessor companies. By a similar series of purchases by Michigan and its various predecessor companies, Michigan acquired and now owns telephone lines in numer-

ous rural communities built by farmers' mutual associations and connected with the exchanges now owned by Michigan. The records of Michigan indicate that at least 46 separate known corporations or organizations have owned some part of the properties now owned by it; that of such 46 predecessors the records of all thereof are either totally lacking or are known to be inadequate for the purpose of determining the original cost of the property now owned by Michigan at the time of the dedication thereof to the public use. It is impossible to segregate property additions constructed since purchase, which property additions have been recorded at cost, but the records of Michigan indicate that it is impossible to determine or estimate, with any satisfactory degree of accuracy, the original cost of at least 80% of the property now owned, which, as of October 31, 1935, was recorded at about $6,402,000.

[fol. 587] Ohio Associated Telephone Company

Ohio Associated Company (hereinafter called "Ohio") was incorporated under the laws of the State of Ohio in 1924 as Ohio Cities Telephone Company. It owns and operates within the State of Ohio 51 local exchanges, serving at least 107 communities throughout the State, there being connected to its exchanges approximately 20,982 telephone stations. All of said exchanges were acquired by said Ohio by purchase. Such exchanges were purchased by Ohio in a series of purchases, with the authorization and approval of the Public Utilities Commission of Ohio, and the properties purchased are recorded on the books substantially at the cost thereof to Ohio in cash or securities.

As stated above, the exchanges now owned by Ohio were acquired through a series of successive purchases by it and its numerous predecessor companies. By a similar series of purchases by Ohio and its various predecessor companies, Ohio acquired and now owns telephone lines in numerous rural communities built by farmers' mutual associations and connected with the exchanges now owned by Ohio. The records of Ohio indicate that at least 38 separate known corporations or organizations have owned some part of the properties now owned by it; that of such 38 predecessors, the records of at least 36 thereof are either totally lacking or are known to be inadequate for the purpose of determining the original cost of the prop-

erty now owned by Ohio at the time of the dedication thereof to the public use; and it is estimated that the original cost of at least 75 per cent of the property now owned by Ohio cannot be determined or estimated with any satisfactory degree of accuracy. The fixed property owned by Ohio as of October 31, 1935 was recorded at $3,750,400.60.

[fol. 588] Pennsylvania Telephone Corporation

Pennsylvania Telephone Corporation (hereinafter called "Pennsylvania") was incorporated under the laws of the State of Pennsylvania in 1897. It owns and operates within the State of Pennsylvania 36 local exchanges, serving some 267 communities within said State, through approximately 49,575 telephone stations. The Company began operations with property constructed by it in Erie, Pennsylvania and certain adjacent territory. In 1926, it acquired the properties of a competing telephone company in Erie and the two were merged. Aside from the property which the Company itself constructed in Erie and the additions which it made to the merged property in Erie, all other exchanges were acquired by said Pennsylvania by purchase.

The properties which have been acquired by Pennsylvania by purchase have at all times been recorded on the books of Pennsylvania at amounts approved by the Public Service Commission of Pennsylvania, such amounts being the cost thereof to Pennsylvania in cash or securities, and properties constructed or additions made to property since date of acquisition have been recorded at the cost thereof.

With the exception of exchanges in Erie, Pennsylvania, all of the exchanges now owned by Pennsylvania were acquired through a series of successive acquisitions by it and its numerous predecessor companies. By a similar series of acquisitions by Pennsylvania and its various predecessor companies Pennsylvania acquired and now owns telephone lines in numerous rural communities built by farmers' mutual associations and connected with the exchanges now owned by Pennsylvania. The records of Pennsylvania indicate that at least 22 separate known corporations or other organizations have owned some part of the properties now owned by it; that of such 22 known predecessors the records of more than 15 thereof are either

[fol. 589] totally lacking or are known to be inadequate for the purpose of determining the original cost of the property now owned by Pennsylvania at the time of the dedication thereof to the public use; and it is estimated that the original cost of at least 54 per cent of the fixed property now owned by Pennsylvania cannot be determined or estimated with any satisfactory degree of accuracy. The fixed property owner, as of October 31, 1935, was recorded at $11,762,780.65.

Tri-State Associated Telephone Corporation

Tri-State Associated Telephone Corporation (hereinafter called "Tri-State") was incorporated under the laws of the State of New York in 1929. It owns and operates within the State of New York 3 local exchanges in at least 3 communities within said State, serving approximately 2,346 stations. All of said exchanges were acquired by said Tri-State by purchase. It is impossible for Tri-State to determine or estimate with any satisfactory degree of accuracy the original cost of the property so acquired, which constitutes approximately fifty per cent of the fixed property now owned by it.

Southwestern Associated Telephone Company

Southwestern Associated Telephone Company (hereinafter called "Southwestern") was incorporated under the laws of the State of Delaware in 1926 as the State Telephone Company of Texas. It owns and operates within the States of Texas, New Mexico, Oklahoma and Louisiana 154 exchanges, serving at least 154 communities within said States, through approximately 20,682 stations. All of said exchanges were acquired by said Southwestern by purchase and were recorded on the books of Southwestern at the cost thereof to Southwestern in cash or securities.

The exchanges now owned by Southwestern were acquired through a series of successive purchases by it and its numerous predecessor companies. By a similar series of purchases by Southwestern and its various predecessor [fol. 590] companies, Southwestern acquired and now owns telephone lines in numerous rural communities built by farmers' mutual associations and connected with the exchanges now owned by Southwestern. The records of

Southwestern indicate that at least 82 separate known corporations or organizations have owned some part of the properties now owned by it; and of such 82 predecessors the records of all thereof are either totally lacking or are known to be inadequate for the purpose of determining the original cost of the property now owned by Southwestern at the time of the dedication thereof to the public service. Although property additions constructed by Southwestern subsequent to 1926 have been recorded at cost, it is impossible to segregate such property additions from property purchased. There is no doubt, however, that it is impossible for Southwestern to determine or estimate with any satisfactory degree of accuracy the original cost of substantially more than half of the fixed property now owned, which was recorded on its books as of October 31, 1935, at $6,266,655.77.

12. The purpose of any system of accounts is to record the facts with respect to the transactions of the accounting company and thereby to portray and reflect the true financial condition and operations of such company. The System of Accounts prescribed by the Interstate Commerce Commission, in accordance with which the accounts of these seven corporations are now kept, achieve this end. The Uniform System of Accounts prescribed by Order No. 7-C, however, prevent the accounting companies from accurately recording the facts with respect to their own transactions and thereby make it impossible for such companies by their accounts to portray and reflect, at all times, their true financial condition and operations. The attempt to comply with said order also will impose on said companies the burden of heavy and unnecessary expenses, and will expose them to [fol. 591] the risk of heavy penalties. The said Order No. 7-C appears arbitrary, unreasonable, confiscatory and beyond the powers vested in the Commission.

This affidavit is made for the purpose of procuring an interlocutory injunction restraining, enjoining and suspending during the pendency of this cause the operation, execution, effect and enforcement of said Telephone Division Order No. 7-C, dated July 19, 1935, effective January 1, 1936, prescribing a Uniform System of Accounts for telephone companies, and for a temporary stay of the opera-

tion of said order to be in effect pending the determination of said motion for said interlocutory injunction.

(Signed) Harold V. Bozell.

Subscribed and sworn to before me this 6th day of December, 1935. Clodagh H. Carter, Notary Public. Notary Public, New York County. N. Y. Co. Clerk's No. 448, Register's No. 70599. Commission Expires March 30th, 1937.

[fol. 592] In opposition to said applications, there was submitted by defendant, Federal Communications Commission, and received, the following:

The affidavit of William J. Norfleet; the affidavit of Robert S. Rains, together with Appendix A thereunto annexed; the affidavit of John H. Bickley; the affidavit of Asel R. Colbert; the affidavit of Malcolm F. Orton; and the affidavit of Charles W. Smith, all verified on the 11th day of December, 1935, and filed herein on the 12th day of December, 1935. Said affidavits respectively are as follows:

[fol. 593] [Title omitted]

AFFIDAVIT OF WILLIAM J. NORFLEET

William J. Norfleet, being duly sworn on oath deposes and says:

I reside at Bethesda, Maryland, and am Chief Accountant of the Federal Communications Commission with offices at Washington in the District of Columbia.

I have been engaged in the field of public utility accounting for the past thirty-one years, of which approximately fifteen years were in the employ of a Class I steam railroad company. During this period I completed a course in accounting and taught classes on that subject. For approximately sixteen years I was employed as an Examiner of Accounts and later as Chief Accountant and Auditor for the Interstate Commerce Commission.

My duties with the Interstate Commerce Commission consisted of making examinations of the general books of accounts and records of many Class I carriers subject to its jurisdiction; the supervision of others engaged in like

examinations; the compilation of reports of such examina-
[fol. 594] tions and of historical and analytical statements therefrom from the dates of organization of the companies to 1914 or later; conducting conferences between carrier and commission representatives with respect to technical and controversial matters involving accounting procedure and practice, and other features pertaining to the requirements of the Commission.

I served as a member of the committee appointed for the purpose of drafting rules and regulations governing the recording and reporting of property changes of steam railroad companies and their cost as adopted by the Interstate Commerce Commission; as an observer and conferee on behalf of the Bureau of Valuation at the public hearings before the Interstate Commerce Commission in Ex Parte 91—General Revision of Accounting Rules for Steam Railroads; Docket 15100—Depreciation Charges of Steam Railroad Companies; Docket 14700—Depreciation Charges of Telephone Companies; and Docket 25705—Accounting Rules for Telephone Companies.

Following the hearings on these matters, I was designated as a participant and conferee in drafting tentative revisions of the accounting rules for steam railroads; in drafting the Interstate Commerce Commission's findings under Docket 15100, and in drafting the Uniform System of Accounts for Telephone Companies prescribed by the Interstate Commerce Commission, First Revised Issue.

Preliminary to the promulgation of the uniform system of accounts prescribed by the Federal Communications Commission, and identified as the Uniform System of Accounts for Telephone Companies, Issue of June 19, 1935, Effective January 1, 1936, hereinafter sometimes referred to as this Commission's system, I participated in the conferences held with representatives of the State regulatory bodies with respect to its provisions.

I examined the requirements of the said uniform system of accounts and considered its provisions from the standpoint of the fundamental needs of uniformity in public utility accounting as a necessary and effective measure of providing a uniform system for recording and reporting data essentially needed as an aid to public regulation and to
[fol. 595] accomplishment of this and without violence to

good accounting practices or to the needs of the company's management, creditors, owners, and other parties at interest. The said system of accounts is particularly directed to the matters of developing, recording, and reporting in a uniform manner accounting data essential to public regulation.

Among my present duties, is the responsibility of advising with and assisting the Commission in the administration and interpretation of the provisions of said uniform system.

I am, therefore, familiar with the intent, purposes, and provisions of said uniform system of accounts.

I have examined the bills of complaint and the affidavits of Messrs. Heiss, Sangster, Young, Kester, Madden, and Bozell, filed in the above-entitled cause.

In view of the foregoing and for reasons hereinafter given, it is my conclusion that the allegations contained in the aforementioned bills and affidavits are predicated in part at least upon misinterpretation of the provisions and that they do not present in their true light, either the requirements or the benefits of the said system of accounts.

I. Original Cost and Telephone Plant Acquisition Adjustment Account

(This corresponds to Item 7 of the Bill of Complaint)

1. This Commission's system of accounts defines "original cost" as applied to telephone plant, franchises, patent rights, and right-of-way, to mean the actual money cost of (or the current money value of any consideration other than money exchanged for) property at the time when it was first dedicated to the public use, whether by the accounting company or by a predecessor public utility.

2. The said system requires that the telephone plant accounts shall be stated on basis of "original cost", as therein defined, and so included in Account 100.1, "Telephone plant in service." The reason for this requirement is the need for continuity and uniformity in accounting for the original [fol. 596] cost regardless of the changes in ownership of the property or the incident of ownership at a given time, and to bring about uniformity in the statement of plant accounts of public utilities. Such continuity and uniformity are essential from the standpoint of charges to operating ex-

penses for depreciation, from the standpoint of passing upon security issues, from the standpoint of considering the reasonableness of the purchase price of property to be acquired, and from the standpoint of valuation for rate-making purposes.

3. A major part of the telephone property now in existence was constructed by or for, and was dedicated to public use for the first time by the present owner. A very minor part of such telephone plant as is now in service was acquired by the present owner through purchase from other public utility companies.

4. In accordance with the accounting regulations in effect since 1913, property constructed for or by the present owner is required to be recorded in the telephone plant accounts at "cost to the accounting company." This Commission's system requires that such property be recorded in the telephone plant accounts at "original cost." In such instances the terms "cost to the accounting company" and "original cost" are of identical meaning.

5. With respect to a minor part of telephone plant now in existence which was acquired by the telephone company from other public utilities, the telephone companies have indulged in optional accounting with the result that certain property so acquired has been included in the plant accounts at "actual cost to the company", other property being recorded by a "merger of the book accounts", other property being recorded at the "current cost new", and still other property at "structural value."

6. This Commission's system requires, on the other hand, that the telephone plant accounts shall be stated on the basis of "original cost" as therein defined. It requires further that the difference between (a) the amount of money actually paid by the accounting company for telephone plant [fol. 597] acquired, and (b) the "original cost" of such property, less the amounts of reserve requirements for depreciation and amortization of the property acquired, and amounts of contributions to the predecessor company or companies for construction and acquisition of such property, shall be recorded in an account entitled 100.4, "Telephone plant acquisition adjustment."

7. Although the plant accounts are now stated as heretofore described, depreciation charges are computed on "book

cost", and retirements are made on "average cost" or "original cost." The Commission's system of accounts corrects these inconsistencies in addition to providing information for the other purposes hereinbefore mentioned, in that it requires all items of telephone plant account to be stated on basis of "original cost" and that depreciation and retirements be computed on the same basis.

8. Plaintiffs allege (page 9) "That as of January 1, 1936, plaintiffs shall restate their then existing property investment accounts by eliminating therefrom the recorded cost or investment of plaintiffs in property theretofore acquired by them from another public utility, and substituting for such recorded cost or investment the amount (estimated if not known) which said property cost some former owner at the date of first dedication to public use."

9. Plaintiffs further allege that the definition of original cost taken in connection with other provisions (not specifically mentioned) of this Commission's system will require in substance and effect that "plaintiffs' property investment accounts shall be kept on a basis which will reflect neither the fact of their actual investment in the property nor the value thereof, but which will conceal the amount of the plaintiffs' actual investment and will substitute therefor, in the case of purchased property, the investment of someone else (estimated if not known) for which plaintiffs had no responsibility. The accounting will thus conceal relevant facts and misrepresent plaintiffs' condition."

[fol. 598] 10. Elsewhere in the bills and in supporting affidavits subsequently filed, the expression "property investment accounts" occurs. Neither the system of accounts now in effect nor this Commission's system, uses the term "property investment accounts" or designates or labels any group of accounts as such. This affiant assumes the term to refer to those accounts of the 200 series designated as "Telephone Plant Accounts." The total of the balances in these accounts are classified in the balance sheet in Account 100, "Telephone plant" under the heading "Investments" in the present system.

11. Under the accounting regulations now effective (instruction 21, page 11), when property in use in telephone service is purchased, the accounting therefor shall be performed by—

(a) Charging the estimated value of land, the current cost new (estimated if not known) of certain other telephone plant, the original cost of certain rights acquired, and the cost of uncompleted projects acquired, to the telephone plant accounts.

(b) Crediting the estimated amounts of depreciation and amortization applicable to the plant to the depreciation and amortization reserve accounts.

(c) Charging or crediting, as appropriate, to Account 278, "Undistributed cost of property" any difference between the foregoing amounts and the cost to the accounting company of the plant acquired.

12. In my opinion Account 278, "Undistributed cost of property", is improperly classified in the present system of accounts as a telephone plant account. It is more appropriately includible as a separate balance sheet account. In many ways it performs the same function as Account 100.4, "Telephone plant acquisition adjustment", prescribed in this Commission's system.

[fol. 599] 13. From the foregoing, it is evident that to determine plaintiffs' investment in telephone plant at the present time with respect to property heretofore purchased from another public utility, it is necessary to consider the amounts entered in the telephone plant accounts for property in telephone service, Account 278, "Undistributed cost of property" and in the depreciation and amortization reserve accounts at time of acquisition.

14. It is therefore apparent that as of January 1, 1936, plaintiffs are not required to eliminate their investment in property acquired from another public utility, from their existing property investment accounts for the reason that such accounts do not comprise, in all instances, their actual investment in such property.

15. Instead of the effect of this Commission's system as above interpreted by plaintiffs, carriers, as of January 1, 1936, will be required to record in the telephone plant accounts and in Account 100.1, "Telephone plant in service", the original cost of their telephone plant in service; in Account 100.2, "Telephone plant under construction", the

original cost of such telephone plant; in Account 100.3, "Property held for future telephone use", the original cost of such property. Any difference between the amounts so recorded and the amounts in the telephone plant accounts and in Account 100, "Telephone plant", at that date whether greater or less than the original cost will be transferred to balance sheet Account 100.4, "Telephone plant acquisition adjustment." In this process, the "catch-all" Account 278, "Undistributed cost of property", will, and properly should be, eliminated from the group of telephone plant accounts.

16. At the present time the telephone plant accounts may be stated on several different bases, as follows:

(a) Cost to the accounting company for that part of their telephone plant constructed by or for them.

[fol. 600] (b) Current cost new at the time of acquisition of certain portions of their property purchased from other public utilities.

(c) Structural value of property acquired from other public utilities.

(d) Cost to the predecessor company in those cases where carriers elected and were authorized to transfer to their books the amounts carried on the books of the predecessor company.

17. After January 1, 1936, under this Commission's system, the basis for all amounts recorded in the plant accounts will be "original cost" only.

18. With respect to property acquired from another public utility, the accounting performed under this Commission's system will disclose, by a simple combination of appropriate accounts, the following information in the accounts of the purchasing company:

(a) The cost of the property to the accounting company.

(b) The original cost (as defined in instruction 3-S. 1 of the uniform system of accounts) of the telephone plant, governmental franchises, and other similar rights acquired.

(c) The amounts of depreciation and amortization applicable to the property represented by item (b) above.

(d) The original cost of telephone plant under construction at date of purchase.

(e) The original cost of property held for future telephone use acquired in the purchase.

(f) The amounts contributed to the predecessor company or companies for construction and acquisition of the telephone plant acquired.

(g) The net of all the foregoing amounts segregated and shown separately in the balance sheet in an account styled 100.4, "Telephone plant acquisition adjustment."

[fol. 601] 19. From the foregoing it is apparent that the accounts and records kept under this Commission's system will disclose not only that essential information reflected in the accounts and records under the present system, but that in addition thereto they will make readily available the essential element of "original cost" of telephone plant at time of first dedication to public use, and that the statement of plaintiffs that accounts kept to conform with this Commission's system "will reflect neither the fact of their actual investment in their property, nor the value thereof, but will conceal the amount of plaintiffs' actual investment and will substitute therefor, in the case of purchased property, the investment of someone else (estimated if not known) for which plaintiffs had no responsibility," is not a correct statement. Contrary to the opinions stated in the bills of complaint and in affidavits filed in support thereof, the provisions of this Commission's system do not violate sound accounting principles and are not arbitrary and unreasonable.

20. Despite the fact that the uniform system of accounts now in effect does not disclose all those essential elements which will be disclosed by this Commission's system, plaintiffs seek to retain said system in effect, and Mr. Sangster in his affidavit (page 17) states, "The Uniform System of Accounts for Telephone Companies, First Revised Issue, prescribed by the Interstate Commerce Commission, is, in my judgment, a system of accounts which is adequate for the aforesaid purposes and, on the whole, is based upon sound principles of accounting."

21. Plaintiffs allege (page 10 of the bill of complaint) that this Commission's system requires that they shall record nothing in their accounts on account of the expense of depreciation with respect to the portion of the property investment which is to be recorded in Account 100.4, "Telephone plant acquisition adjustment", and (page 11, Par. C) that the system prevents them from recording in their expense accounts the expense of depreciation which they actually incur. These allegations appear to be directed against something which the Commission proposes to do in [fol. 602] the future. With respect to amounts represented in Account 100.4 "Telephone plant acquisition adjustment," there is nothing in this Commission's system which precludes charging to operating expenses such amounts as may be appropriate according to the character of the item.

22. Affiants for plaintiffs say that the amounts to be recorded in Account 100.4 must be extinguished either immediately or later at the pleasure of the Commission, and that such amounts are a deferred charge against surplus, since the Commission can make it such a charge at any time. This is purely speculative and unsupported by the system of accounts, the general rules of which govern the disposition of items not specifically provided for. The affiants may just as well have made the proper assumption, namely, that the disposition of the amounts to be recorded in Account 100.4, "Telephone plant acquisition adjustment" would be disposed of, after the character of the item had been determined, in a manner consistent with the general rules underlying the uniform system of accounts for the distribution of expenditures, according to their character, to operating expenses, income, surplus, or remain an investment.

23. The Commission's system of accounts looks specifically to allowing telephone companies to recover, through charges to operating expenses for depreciation, the "original cost" of depreciable property. It also looks to segregating such "original cost" from the cost of acquiring property from predecessor companies and further to the recovery of the differences, if the conditions and circumstances contributing to such differences warrant recovery, through charges to operating expenses for amortization.

24. Plaintiffs stated (page 11, par. (b) of their bill) that this Commission's system requires them "to write off a portion of their actual investment, even where the price paid was the actual value of the property and where there has been no change in value, thus requiring them to record a loss on their books when in fact they have suffered no [fol. 603] loss. A similar writing off of a loss which has not been incurred will be required of plaintiffs whenever in the future they may purchase property at a price which, although representing its actual value, is higher than its cost to the predecessor public utility which first dedicated it to public use."

25. There is nothing in this Commission's system to justify the statement of plaintiffs that they are required to record a loss on their books when in fact they have suffered no loss.

26. Plaintiffs allege (page 11, par. (b)) that the requirements of this Commission's system are impracticable of application in their accounting; that they would necessitate establishing the identity of items of purchased property many years after the purchase when many of the purchased items have been retired and when the surviving items have been so commingled with the previously owned and subsequently constructed plant that their identification would be impossible; that they would necessitate estimating the original cost at the dates of installation of such items because in many cases books and accounts were not kept in such a manner as to show such original cost at dates of installation; plaintiffs further allege that these difficulties would complicate their retirement accounting and would add greatly to the accounting expense and would result in their accounts reflecting in part unreliable estimates instead of facts.

27. This Commission's system recognizes the fact that plaintiffs may encounter difficulty in identifying in the accounts and records, the original cost of some of the property which was acquired by purchase from a predecessor public utility and is now in existence in telephone service. Provision has been made for such difficulties by stating in the text of Account 100.4, "Telephone plant acquisition adjustment", that if the actual original cost is not known,

the entries in this account shall be based upon an estimate of such costs. A similar provision appears in instruction 21 on page 12.

[fol. 604] 28. Congress was aware of the fact that present necessity would in all likelihood require estimates to be made in lieu of recorded facts and made special provision to authorize such procedure and endowed upon the Commission the power to require of the plaintiffs the information desired.

29. Section 213(c) of the Communications Act of 1934, provides as follows:

The Commission may at any time require any such carrier to file with the Commission a statement showing the original cost at the time of dedication to the public use of all or of any part of the property owned or used by said carrier. For the showing of such original cost said property shall be classified, and the original cost shall be defined, in such manner as the Commission may prescribe; and if any part of such cost cannot be determined from accounting or other records, the portion of the property for which such cost cannot be determined shall be reported to the Commission; and, if the Commission shall so direct, the original cost thereof shall be estimated in such manner as the Commission may prescribe. If the carrier owning the property at the time such original cost is reported shall have paid more or less than the original cost to acquire the same, the amount of such cost of acquisition, and any facts which the Commission may require in connection therewith, shall be reported with such original cost. The report made by a carrier under this paragraph shall show the source or sources from which the original cost reported was obtained, and such other information as to the manner in which the report was prepared, as the Commission shall require.

30. In view of the above quotation provisions have necessarily been included in the uniform system of accounts so that when, in the future, information specified by the Congress of the United States is desired it will be available, instead of subject to the very arguments of the plaintiffs that, since it is not available as complete and accurate record of fact, it should be ignored.

31. Incidentally, the recording of items in the accounts, and particularly the telephone plant accounts, on basis of estimates is not an innovation in public utility accounting. The accounting now performed by plaintiffs for depreciation and for employees' pensions is almost exclusively based upon estimates.

[fols. 605-607] 32. Plaintiffs allege in their bill (page 12, par. (e)) that the requirements of this Commission's system compel them to make radical changes in their completed accounts, and that the Communications Act does not empower the Commission to prescribe retroactive changes in accounts which have been lawfully and correctly kept, but only to prescribe the forms of accounts, records, and memoranda to be kept in the future.

33. All that is required in this respect by this Commission's system is a reclassification of balances as of its effective date in certain balance sheet accounts. Similar reclassifications have been made in the past and are necessary when any system is installed or revised.

34. Plaintiffs allege (pages 9 and 10 of their bill) that this Commission's definition of original cost, taken in connection with other provisions (not specifically mentioned) of said system of accounts, is "so entirely contrary to fundamental principles of correct accounting and [illegible] arbitrary and unreasonable as to amount to an abuse of the Commission's power, are beyond the statutory power and authority of the Commission, and are illegal and void, * * *."

35. General accounting principles and practices, fortified by court decisions, recognize "original cost", as defined in this Commission's system, as a proper element in the determination of valuation for rate-making purposes and an appropriate base for depreciation charges. It is customary in uniform systems of accounts, just as in many statutes, to attach a definition which suits the immediate requirement for a brief descriptive term needed with respect to an element appearing fundamentally and frequently in the document at hand. In the case of this uniform system, the definition naturally has been chosen which furnishes an apt description of that certain aforementioned type of element so significant in utility regulation. "Original cost" as de-

fined in the Commission's system is not an innovation in the field of public utility accounting.

* * * * * * *

[fol. 608] III. Differentiation Between Items to Be Recorded in Account 100.1 "Telephone Plant in Service", Account 100.3, "Property held for Future Telephone Use", and Account 103, "Miscellaneous Physical Property." (This Corresponds to Item 9 of the Bill of Complaint.)

1. There is nothing in the accounting system prescribed by this Commission to justify the statement of plaintiffs that the dividing lines between Accounts 100.1, "Telephone plant in Service," 100.3, "Property held for future telephone use", and 103, "Miscellaneous physical property", are so indefinite and ambiguous that it would be impossible for plain iffs to know to which account substantial amounts of their property should be charged.

[fol 609] 2. The nature of the properties to be recorded in these respective accounts are specifically set forth in the text thereof. (See pages 26, 27, 28, and 29 of the Uniform System of Accounts prescribed by this Commission.)

3. There may develop so-called "border-line" cases calling for interpretations of the pertinent accounting regulations. This is true with respect to the provisions of any system of accounts which, in general terms, must cover a broad field of activities and has been and is true of the system of accounts prescribed by the Interstate Commerce Commission which plaintiffs seek to retain. A familiar illustration of the necessity for such interpretations, known to all persons familiar with accounting, is the distinction between capital and revenue expenditures. The problem of diffentiating between entries to be made in Accounts 100.1, 100.3, and 103 here discussed, is, in my opinion, comparatively simple and amply provided for by the explicit instructions contained in this Commission's system of accounts.

4. In the event that plaintiffs or other telephone companies may desire assistance or advice of this Commission in classifying any item to be recorded in their accounts, they may submit all questions of doubtful interpretation

of prescribed accounting to this Commission for consideration and decision as provided in instruction 9 of this Commission's system of accounts. For more than twenty years, it has been the common practice of plaintiffs and other telephone companies to follow this procedure in submitting to the Interstate Commerce Commission or this Commission numerous inquiries requesting such interpretations relating to accounting regulations.

5. It is significant that the plaintiffs have submitted no inquiries to this Commission with reference to an interpretation of the above accounts. In view of the facts mentioned in the next preceding paragraph, there is no reason- [fol. 610] able basis for any accounting official of plaintiffs to conclude or believe that they will be required to make any accounting entry "at their peril" by reason of this Commission's system of accounts. To the contrary, they have every reason to believe that this Commission will lend all needful assistance in the practical and reasonable application of its accounting regulations.

6. The language used in the text of the accounts above complained of is and has been long in use and understood in the public utility field by those professionally interested in these matters and, in my opinion, is neither contrary to fundamental practice of accounting, arbitrary, nor unreasonable.

IV. Depreciation of Spare Plant. (This Corresponds to Item 10 of the Bill of Complaint)

1. Plaintiffs take the position that spare plant will, under this Commission's system of accounts, be classified in Account 100.3, "Property held for future telephone use" and that plaintiffs will be deprived of such depreciation (as an operating expense) as may accrue during the periods when such property is classified in said Account 100.3.

2. The provisions contained in this Commission's system of accounts do not warrant the assumption of plaintiffs that their necessary spare plant should be classified in said Account 100.3.

3. It is my opinion and understanding that this Commission's system of accounts permits the recording of necessary "stand-by" plant in Account 100.1, "Telephone plant

in service" and that periodical transfers between said Account 100.1 and Account 100.3, "Property held for future telephone use" will not be required by reason of seasonable changes or fluctuating demands for plaintiffs' services. It is also my understanding that such interpretation was discussed and made clear at the conference between representatives of this Commission and representatives of plaintiffs and other telephone companies relating to the then proposed system of accounts for telephone companies, on May 16, 1935.

[fol. 611] 4. Furthermore, it is my understanding that, under this Commission's system of accounts, it is not intended that plaintiffs will be deprived of the right to recover, through charges to operating expenses for depreciation, the original cost of their necessary spare plant.

V. Accounting for Expenditures in Excess of Just and Reasonable Amounts. (This Corresponds to Item 11 of the Bill of Complaint)

1. This Commission's system of accounts requires that all charges to the accounts prescribed for plant investment, income, operating revenues, and operating expenses shall be just and reasonable and that payments by companies in excess of such just and reasonable charges shall be charged against Account 323, "Miscellaneous income charges." This requirement does not introduce into the accounting field any new matter.

2. It is contemplated that the charges to accounts immediately affecting revenues and rates shall be just and reasonable. The accounts of telephone companies, for example, include interest during construction period on general funds expended for the acquisition and construction of property. These interest charges shall be on a reasonable basis. The accounts also include charges for general services and licenses, and for services rendered under license agreements providing for the furnishing of general accounting, engineering, financial, legal, patent, and other general services. Such charges may be paid by one company and apportioned among two or more companies. It

is essential that such charges and such apportionment be just and reasonable.

VI. Adequacy of Accounting System Prescribed by This Commission to Become Effective January 1, 1936. (This Corresponds to Item 12 of the Bill of Complaint)

1. Plaintiffs allege (page 16) in their Bill of Complaint that this Commission's system of accounts makes it impossible for them to keep accounts adequate for the information of their officers and directors and for making true representations to prospective investors, as well as for the information of their existing stockholders or their security holders.

[fol. 612] 2. In my opinion, this is not a statement of fact as evidenced by the remarks heretofore made with respect to the other allegations in the Bill of Complaint. It is also my opinion that this Commission's system of accounts will disclose not only the essential information now disclosed by the system of accounts in effect but that it will furnish additional information essential to this Commission and to other parties of interest, and that the accounts kept under the system will more truly reflect plaintiffs' financial conditions.

VII. Separability of Provisions Complained of From Other Provisions of This Commission's Accounting System. (This Corresponds to Item 13 of the Bill of Complaint)

1. Plaintiffs allege (page 17) in their Bill of Complaint that it is impossible, practically or legally, to separate the provisions which effectuate the requirements of this Commission's system of accounts complained of therein from other provisions of the system.

2. In my opinion, this is not a statement of fact. For example, if the court in its judgment should decide that instruction 2-B.1, covering just and reasonable charges, and the fourth ordering clause of Telephone Division Order No. 7-C which requires that the basis of comparison with the prior year shall be maintained, to which plaintiffs complain in allegations numbered 11 and 14, be lifted bodily

from this Commission's system of accounts, the completeness of the system will be maintained. It is therefore evident that the statement made by plaintiffs at this point and in the supporting affidavits, is not a statement of fact.

* * * * * * *

[fol. 613] IX. Expense to Telephone Companies of Adjusting Records to Comply With This Commission's Accounting System

1. The statements in the Bill of Complaint and in the supporting affidavits regarding the estimated expense to plaintiffs of adjusting their records to comply with the accounting system prescribed by this Commission to become effective on January 1, 1936, are, in my opinion, far in excess of the actual costs which will be experienced in such change. This statement is based on my knowledge of the accounts affected and the changes required.

* * * * * * *

[fol. 614] In my opinion and for the reasons heretofore mentioned, the requirements of this Commission's system of accounts are in no way contrary to fundamental principles of correct accounting but are, in fact, in conformity therewith and are neither arbitrary nor unreasonable.

William J. Norfleet.

Subscribed and sworn to before me this 11th day of December, 1935. Stephen Tuhy, Jr., Notary Public. My Commission expires 10-23-38.

[fol. 615] [Title omitted]

AFFIDAVIT OF ROBERT S. RAINS

CITY OF WASHINGTON,
District of Columbia, ss:

Robert S. Rains, being duly sworn on oath, deposes and says:

I reside at 1819 G Street, N. W., Washington, District of Columbia.

I am a Certified Public Accountant (California).

From the years 1908 to 1933, inclusive. I was in the Public Accounting profession. A resume of my accounting experience and qualifications is shown in Appendix "A" attached hereto and made a part hereof.

During this period, I have performed special accounting services for some of the country's leading Financiers and Capitalists, and for many of the largest and most outstanding Financial, Industrial, and Public Utilities Corporations in the United States. I have made cost and financial studies, installed financial, production, cost systems and methods, and manufacturing budget controls. I also made investigations of cost systems and methods, procedures, depreciation accounting, which included reserves for depreciation, and all the elements which enter into the computation of equitable reserves for factors such as obsolescence, depletion, etc.

[fol. 616] A brief record of my accounting career from the year 1908 to the present year, 1935, is as follows:

1908 to 1916, inclusive—Member of the staff of the nationally known Public Accounting firm of Price Waterhouse and Company, California and New York, and in the latter part of this period I was Managing Senior of the staff.

1917 and 1918—Managing Senior of the staff of the Public Accounting firm of Arthur Young and Company, New York City and Chicago, Illinois.

1919—Partner in the Public Accounting firm of Harris Latter and Company, New York City and Chicago, Illinois.

1920—Partner in the Public Accounting firm of Strachan and Rains, consolidating at the end of the year with Mattingly and Nutt, Tax Consultants.

1921 and 1922—Partner in the firm of Mattingly and Nutt, Tax Consultants and Auditors, New York City; Columbus, Ohio, and Los Angeles, California.

1923 to 1926, inclusive—Managing Senior of the staff of the Public Accounting firm of Stagg, Mather and Company, New York City and Havana, Cuba.

1927 and 1928—Partner in the Public Accounting firm of Cooper, Rains and Company, Tampa, Florida.

1929 to 1933, inclusive—Partner in the Public Accounting firm of R. S. Rains and Company, New York City, and Philadelphia, Pennsylvania.

In August, 1933, through Mr. Henry P. Seidemann, C. P. A., and Chief Consulting Accountant, Institute for Gov-

ernment Research of the Brookings Institution, Inc., I was appointed in the United States Department of Agriculture, Agricultural Adjustment Administration, to assist him in the organization of the Agricultural Adjustment Administration. I was later made Chairman of the Committee on [fol. 617] Organization and Procedure, Office of the Comptroller, A. A. A., which position I held to the date of my resignation July 8, 1935.

On July 9, 1935, I was appointed Special Consultant on all Accounting activities of the Accounting, Statistical and Tariff Department of the Federal Communications Commission. This position I now hold.

In my capacity as Special Consultant of the Accoounting, Statistical and Tariff Department of the Federal Communications Commission, I am thoroughly familiar with the Classification of Accounts for Telephone Companies, Issue of June 19, 1935, Effective January 1, 1936, and am fully acquainted with the matters contained in the bills of complaint as well as the statements made by the expert witnesses.

1. It is mandatory upon this Commission that the Orders promulgated by it be such as to give full recognition to the equitable interests of all parties concerned. It is recognized that the facts set forth in the bills of complaint represent the viewpoint of the utility owners or stockholders. The above mentioned classification of accounts has been designed to provide a just and reasonable practice in this respect.

2. The complaint of the plaintiff takes exception chiefly to that section of the Uniform System of Accounts, Issue of June 19, 1935, Effective January 1, 1936, which states that purchased property shall be recorded in the telephone plant accounts at the original cost of the property at date of dedication to public service. The difference between (a) the amount of money actually paid for the property; and (b) the original cost of such property, less accrued depreciation and the amounts of contributions to the predecessor company, shall be debited or credited, as appropriate, to account 100.4 "Telephone Plant Asquisition Adjustment", later to be disposed of as the Commission may direct.

3. The correct valuation to be given purchased property has long been a disputed point between public utilities and

regulatory bodies. Plant may be purchased for various reasons such as, for the elimination of competition, to acquire active prosperous property, or for development or [fol. 618] reconstruction of an existing plant. That cost of plant purchased should be borne by the subscribers in all instances does not appear justifiable. No rigid regulations can be established which would administer an equitable settlement of all situations in the best interests of both subscribers and utility owners.

4. Sound accounting practice and principles supported by court decisions, dictate cost as the proper basis for valuation and depreciation charges. This entire question hinges on the correct definition of cost. The present position taken by some regulatory bodies is that cost means the actual money cost, or the current money value of any consideration other than money exchanged, for property at the time it was first dedicated to the public use. This engenders the reasoning that subscribers should not be assessed additional costs because title to the property changes hands during its service life. The companies contend that cost is the actual price they pay for property at the time of purchase and that all purchases of property should be borne by the subscribers through depreciation expense.

5. The first uniform system of accounts, effective January 1, 1913, provided that purchased property should be recorded at the purchase price, if not in excess of structural value, otherwise at structural value. These provisions were changed by the revised uniform system of accounts, effective January 1, 1933, in that purchased plant was recorded at current cost new, less accrued depreciation, and depreciation was computed on that basis.

6. Throughout their complaint, the plaintiffs infer that the excess of purchase price over original cost less accrued depreciation will always represent a loss to the stockholders. Such an inference is decidedly a misconstruction of facts. Those amounts set up in account 100.4, „Telephone Plant Acquisition Adjustment", will be disposed of according to the findings of the Commission and will result in a loss to the utility stockholders only in those cases where such loss exists and should be borne by the stockholders. In my opinion, this elastic regulation will provide more

accurate and dependable information for this Commission's purposes.

[fol. 619] 7. The plant accounts of the plaintiffs under regulations heretofore prescribed by the Interstate Commerce Commission may now include:

1. Current cost new at the time of acquisition by plaintiffs of some parts of their plant bought from other public utility companies.

2. Structural value, this may be either original cost at the time of first dedication to public use or current cost new when acquired by the plaintiffs.

3. Original cost at time of first dedication to public use for plaintiffs' property constructed by them or for them.

4. Original cost at the time of first dedication to public use by a predecessor company, or actual cost to that company.

This variation of costs is not sound accounting. The telephone plant accounts, including the above various costs are now used in computation of depreciation charges to operating expenses.

Allegation 7 (a). Objections to Original Cost Basis

8. The showing of the carrier's investment in telephone plant on the four bases enumerated above is confusing and contrary to sound public utility accounting. The method of accounting which will be effective on January 1, 1936, will more truly show the plaintiffs' condition than is now reflected by accounting performed under present regulations. The telephone plant amounts will be recorded on a uniform basis. The present method of accounting may result in inflating property values simply because the title to property changes hands.

Allegation 7 (b). Plaintiffs Would be Required to Record a Loss for That Amount by Which Purchase Price Exceeds Original Cost

9. There is no statement in the Uniform System of Ac- [fol. 620] counts, Effective on January 1, 1936, which provides that a purchasing utility shall record a loss on their

books where the price paid was the actual value of the property purchased. The purchase price of telephone property does not necessarily represent the true value of the property insofar as the user of the property is concerned. The purchase price may involve a consideration for items on which carriers are not entitled to earn a return on investment or recover its investment through depreciation charges borne by consumers.

10. Plaintiffs may have property which has been transferred between its affiliated companies by purchase and sale at a valuation greater than original cost. It is contended that a utility acting on its own initiative in purchasing property should bear excess costs incurred thereby rather than the subscribers who happened to be located in that territory. Stating this property at original cost will not result in a loss to the stockholders since they only realized a book profit at the time the property was transferred. Purchases from independent companies at values far above books costs may include good will or considerations for the surrender of competitive territory.

Allegation 7 (c). Depreciation Expenses

11. There is nothing in the proposed System of Accounts to prevent appropriately charging to operating expenses all depreciation losses which have occurred.

Allegation 7 (d). Cost of Ascertaining Original Cost Figures Prohibitive as well as Impossible of Procurement

12. In those cases where the original cost of the property which was acquired by purchases from a predecessor public utility, and is now in existence in telephone service, the cost of which is not known, provision has been made in the text of account 100.4 "Telephone Plant Acquisition Adjustment", that such cost shall be estimated. Estimations of such costs have been arrived at with reasonable success in [fol. 621] other lines of public utility regulation such as the Interstate Commerce Commission's valuation of railroad properties.

13. Affiant for plaintiffs estimate that telephone plant valued at approximately $750,000,000 has been acquired by

purchase, of which over $500,000,000 or more than two-thirds has been purchased from affiliated and subsidiary companies. The records of the affiliated and subsidiary companies should be available for determination of the original cost of such purchased property.

14. Congress, in framing and passing the Communications Act of 1934, indicated "original cost" as an important factor to which the Federal Communications Commission should give its attention.

15. Continuation of an improper accounting system can not be justified merely because of the difficulty involved in transposing such a system to a proper accounting basis.

Allegation 7 (e). Commission Not Empowered to Require Retroactive Changes in Accounts

16. Changes are not required in completed accounts which would result in adjustment of Financial Statements of past accounting periods. Only such adjustments would be made in existing open accounts which bear, on future acounting of the telephone companies subject to the order.

Allegation 7 (f). Issuance of Individual Orders to Individual Carriers Unlawful

17. The requirement of the uniform system of accounts that the amounts recorded in account 100.4 "Telephone plant acquisition adjustment" are to be disposed of, written off, or amortized in such manner as the Commission may direct, as to each individual property acquisition, is necessary in order that limitations may not prevent proper regulation. Where the accounts of utilities of different sizes and with different business practices and policies involve the purchase of property from predecessor companies and such acquisitions are made through the exchange of [fol. 622] securities or properties, the issuance of individual orders requiring an individual carrier to make specific entires with respect to transactions as to which it has made no general accounting rules, regulations or classification is imperative.

* * * * * * *

Allegation 9. Ambiguity of Instructions with Reference to Accounts 100.1, 100.3, and 103 Compels Plaintiffs to Make Entries at the Peril of Penalty

20. The text of account 100.1, "Telephone plant in service", provides that this account shall include the original cost of the company's property used in telephone service at the date of the balance sheet. The text of account 100.3, "Property held for future telephone use", provides that this account shall include the original cost of property owned and held for immiment use in telephone service. The text of account 103, "Miscellaneous physical property", provides that this account shall include the company's investment for physical property other than property the investment of which is includible in account 100.1, "Tele- [fol. 623] phone plant in service"; 100.2, "Telephone plant under construction", and 100.3 "Property held for future telephone use".

21. Statements of plaintiffs that the dividing line between these classifications are so indefinite and ambiguous that it will be impossible for plaintiffs to know to what account substantial amounts of their property should be charged is presumably based upon their efforts to interpret the language used in the text of these accounts.

22. Instruction 9 on page 8 of the proposed system provides that to the end that uniformity of accounting may be maintained, the company shall submit all questions of doubtful interpretation of the prescribed accounting to this Commission for consideration and decision. If there is doubt in the minds of plaintiffs as to the interpretation to be placed on the language used in the text of the aforementioned accounts, dictates of propriety suggest that the company comply with this instruction.

* * * * * * *

Allegation 12. Radical Changes in Financial Statements for Publication Would Seriously Impair Plaintiff's Credit

24. It is necessary that the plaintiffs keep books of account that will accurately record the facts of their transactions and truly reflect their true status. No accounting system should be so designed as to conceal relevant facts

or to misrepresent the true condition of any business. In my opinion, this Commission's system of accounts is so designed as to accurately record essential facts of the transactions of telephone companies and to reflect the true status of their condition.

[fols. 624 & 625] Allegation 13. Contention that Uniformr System of Accounts Is Interdependent and Nonseverable

25. The Federal Communications Commission is authorized to prescribe changes in the manner of keeping records by Section 220 (a) of the Act. Should the Court in its judgment find any one of these provisions illegal, such provisions can be corrected without detriment to all other provisions of the Uniform System of Accounts.

* * * * * * *

[fol. 626] (Sgd.) Robert S. Rains.

Subscribed and sworn to before me this 11th day of December, A. D. 1935. (Sgd.) Stephen Tuhy, Notary Public. Com. expires 10-23-38.

[fol. 627] APPENDIX "A" TO AFFIDAVIT

Resume of Accounting Experience and Qualification

National Lead Corporation
American Locomotive Company
General Cable Corporation
American Brass Company
Florida Power and Light
Bureau of Power and Light (Los Angeles, Calif.)
American Foundries
Brooklyn-Manhattan Transit Corporation

Cost studies, and reports thereon. Associated with me in making these cost studies was my former associate and partner, Mr. Frederic W. Kilduff, author of the following well known books on accounting subjects: "Inventory Practice and Material Control", and "Accounting and Auditing Handbook". Both books are published by McGraw-Hill Company.

San Juaquin Light and Power Co., Fresno Calif.
Pacific Gas and Electric Co., Los Angeles, Calif.

Installation of Estimate Budget Control and Financial Construction cost system of Transmission Lines, also installed new Construction Cost Department.

Cuban American Sugar Co., New York and Cuba

For three years during the months of October and November I went to Cuba to make the annual audit of the above company and its subsidiaries, the Chapara Sugar Co., San Manuel Sugar Co., Chapara Light and Power Co., Chapara Water Co., returning to New York to audit the Cuban American Sugar Company's New York Office, and upon completion of same, prepared the financial report for the fiscal year. Also reorganized Cost Production and Financial systems.

[fol. 628] National Conduit and Cable Company, Hastings, N. Y.

Installation of cost systems and methods, production and financial systems. Engaged by Mr. H. J. Pritchard, President of the company.

Fischer, Sweeney Casting Co., Hoboken, N. J.

Installation of the cost, production and financial systems, work performed for Mr. H. J. Pritchard, President, National Conduit and Cable Company, who was financially interested in the Fischer, Sweeney Casting Company.

U. S. Steel Corporation, Gary, Indiana.

Special cost investigation and recommendation of changes, which were accepted.

Stone and Webster Corporation, Boston, Mass.

Investigation of the financial condition and cost of the D. P. Davis Properties, Tampa and St. Augustine, Florida. Upon completion of same, Stone and Webster took over the properties and requested me to assist them in the reorganization. After the reorganization had been completed, Stone and Webster formed a subsidiary company,

for financing and construction. Was made Vice-President and Treasurer of the corporation. On Davis Island, Tampa, Florida, this corporation constructed the Mirsol Hotel, Palmerin Hotel, Davis Island Country Club, and thirty-eight high type Spanish houses; also The Orange Grove School building for the city of Tampa Florida, and the Post Office building for the United States Government at Lakewood, Florida.

Investigation of the cost of construction of the Big Creek Dam, Fresno, California.

Ford, Bacon and Davis, Engineers, New York, N. Y.

Investigation of cost, production, and financial systems of the Virginia-Carolina Chemical Company, Richmond, Virginia.

[fol. 629] George W. Goethals and Co., New York, N. Y.

Special investigations of corporations requiring refinancing, and investigation of cost system of the Splitdorf Electric Corporation, Newark, N. J., and recommendation in changes of cost system, which was accepted.

Tide Water Oil Company, New York, N. Y.

Investigation of depletion and reserves therefor, of the numerous properties owned by the Tide Water Oil Company.

Consolidated Car and Heating Company, Albany, N. Y.

Reorganization of the cost, production and financial systems; remaining in charge until new systems were properly operated.

Cerro De Posco Copper Corporation, New York, N. Y.
Green C. Copper Company, Mexico
Globe Mining Company, Globe, Arizona

Special investigations of mining costs and depletion reserves.

Sperry Aircraft Co., Farmingdale, L. I.

Entire installation of cost, production and financial systems and Consulting Accountant to Mr. Lawrence Sperry, until the time of his death.

Canadian Car and Foundry Company, Montreal, Canada
American Car and Foundry Company, New York, N. Y.

Special investigations of cost and production systems with recommendation for revision.

Ford Motor Company, Detroit, Michigan

I was selected by Mr. Dawd of Jones, Addington and [fol. 630] Caesar, attorneys for the Ford Motor Co., to gather cost data from certain process manufacturing plants throughout the country, covering a certain process. The reason for this investigation was that the Parker Process Company was suing the Ford Motor Co. for infringing on their patents and claiming royalties and damages for the use of same. The Chief Chemist of the Ford Motor Co. and myself spent several months gathering facts. The Chief Chemist examined the various secret processes used by these different plants, while I built up the costs relating to these secret processes. The plants that extended the courtesy of inspecting the various operations and costs pertaining to same were:

General Electric Co., Schenectady, N. Y.
Western Electric Co., Chicago, Ill.
The Stanley Works, New Britain, Conn.
North & Judd, New Britain, Conn.
New Haven Sheradizing Co., Hartford, Conn.
Yale & Towne, Stamford, Conn.

Pennsylvania Railroad Company, Philadelphia, Pennsylvania

Special investigation relating to costs systems and methods of various subsidiary companies. Engaged by Mr. F. J. Fell, Jr., Vice-President and Comptroller of the Pennsylvania Railroad Company.

The Baldwin Locomotive Works, Philadelphia, Pennsylvania

Special investigation of cost systems and methods of subsidiaries of Cramp Morris Industrials, Inc. Engaged by Mr. Carl F. Noyes, Comptroller, Baldwin Locomotive Works.

B. F. Goodrich Co., Akron, Ohio

For three years had full charge of annual audit, preparing consolidated balance sheet, profit and loss, and surplus account, consisting of eighteen subsidiary companies (eight [fol. 631] domestic and ten foreign). During the year 1925, installed the Budget Control System for the entire Akron plant and its subsidiaries. Also revised the cost and production systems at the Akron plant.

Moto-Meter Company, Long Island, New York

Thorough investigation of cost systems and recommendations of changes, which were accepted.

Remington Arms U. M. C. Company, Bridgeport, Connecticut

The installation of the cost, production, and financial sysems, accounting methods and depreciation accounting. The company employed at the time twenty thousand persons. Had with me on this work twenty-two assistants. Subsequent to the complete installation of the systems and methods, personally supervised the contracts existing between the Remington Arms Company, and the English, French, and Russian Governments. Attended monthly meetings of the Board of Directors of the Remington Arms Company. The Directors were H. S. Kimball, John Pryor, Percy Rockfeller, Frank H. Dodge, C. S. Hawley and Mr. Tyler. Also held conferences with the officials representing the English, French and Russian Governments.

United States Government, Ordnance Department

Have the distinction of being the first Public Accountant in the United States to represent this Government on plants, which the Government commandeered, having full charge of the investigation of the Liberty Ordnance Company, Bridgeport, Connecticut, which Company had contracts from both Army and Navy. My instructions from the Ordnance Department were to render a report showing what profits the Liberty Ordnance Company was making, dividing the profits between the contracts on hand, estimating the cost of completing each of the contracts on hand, thereby showing approximately what profit would have

been made under each contract had the Company been able to complete these contracts. Prepared the case for the [fol. 632] Government together with General Charles C. Jamieson, Col. Griggs, and Capt. Carlin. Representing the Liberty Ordnance Company were Senator McNeil and the Hon. Homer S. Cummings. The judges of the court were Col. Robert R. Montgomery and Col. Dean.

United States Government—Department of Justice

Special investigations made for the Honorable James Cameron, Director of Accounting Investigations, War Frauds Section.

United States Shipping Board

Investigation of the financial condition and voyage costs of the Italian Star Line Company and report thereon submitted to U. S. Shipping Board, Washington, D. C.

United States Government—War Department—Aircraft Contracts

Investigated the expenditures and receipts on cost plus motor contracts of the Wright Martin Corporation, New Brunswick, New Jersey. Work performed for the Hon. Charles E. Hughes, Chairman, Special Investigation Committee, Aircraft Contracts.

J. P. Morgan and Company, New York, N. Y.

Investigation of the cost and production systems and financial conditions of the New York Evening Post, for the purpose of purchase by a syndicate headed by Mr. Thomas W. Lamont.

When J. P. Morgan and Company purchased the controlling interest of the Haviland China Company from Mr. George Haviland, the undersigned reorganized the entire cost, production and financial system for the Morgan interests.

[fol. 633] Mr. A. Barton Hepburn, Formerly Chairman of the Board of Directors, Chase National Bank, New York, N. Y.

Private investigations for Mr. Hepburn pertaining to corporations desiring to float bond issues. Investigations

included capital structure, accounting methods, cost systems, depreciation and appreciation in the prices of properties, equipment or intangibles.

Mitsui Company and Mitsui Bank, New York, N. Y.

Thorough investigation of the cost and productive systems and financial conditions of the Standard Aircraft Company's plants located at Elizabeth and Plainfield, N. J. Work performed for the Board of Directors of the Mitsui Bank.

National City Bank, New York, N. Y.
State Bank, New York, N. Y.
North City Trust Company, Philadelphia, Penna.

Special investigations of capital structure. Accounting methods, depreciation accounting, and cost and production systems of firms desiring to make large loans, or float bond issues.

Associated Producers, Inc., Los Angeles, California, and New York, N. Y.

When Thomas Ince, Mack Sennett, Allan Dwan, J. Gardner Sullivan, J. Parker Reed and other producers formed the Associated Producers, Inc., I installed the entire cost, production and financial systems and methods. Was one of the first Public Accountants to install cost and production systems for the Motion Picture Industry. My first assignment was the World's Film Corporation, being engaged by Mr. William A. Brady, President of the Company.

General Ice Cream Company, Schenectady, N. Y.

Investigation of the cost, production and financial sys- [fol. 634] tems of the Utica Ice Cream Company, Purity Ice Cream Company and Syracuse Ice Cream Company, prior to the merger with the General Ice Cream Company. Reorganization of cost production systems and installation of new financial, branch and budget control systems after the merger.

Huyler's Candy, New York, N. Y.

Reorganization of cost and production systems at factory and installation of branch stores accounting system.

McKesson and Robbins, Inc., New York, N. Y.

Reorganization of entire cost, production and financial systems.

Windsor Print Works, North Adams, Massachusetts
Columbia Mills, Inc., New York, N. Y.
Cravenette Company, New York, N. Y.

Special cost investigation at plants and recommendations of changes, which were accepted.

Utah Construction Company, Ogden, Utah
Twohy Bros. Construction Company, Portland, Oregon
Joseph F. O'Brien Construction Company, San Francisco, California
E. B. & A. L. Stone Construction Company, Oakland, California

Installation of contractor's construction cost systems for cases assigned to him with a view to determining whether all merchandise has been accounted for and all assets turned over to the Receiver.

Estate of James B. Haggin, New York, N. Y.

Upon the death of James B. Haggin, President of the Cerro de Pasco Copper Corporation, I was selected to make the accounting for the estate, and upon completion of same, report was submitted to Mr. L. T. Haggin, Executor for the estate. Also preparation of estate taxes.

[fol. 635] H. B. Claflin and Co., Inc., New York, N. Y.

Investigation of the H. B. Claflin & Company, Inc., bankruptcy. After bankruptcy reorganization, installation of new cost systems were effected. This work was performed for A. D. Juilliard, Receiver.

Hirsch Lillienthal and Co., New York, N. Y.
Block Maloney and Co., New York, N. Y.
Pouch and Company, New York, N. Y.
Farr and Company, New York, N. Y.

Annual audits of the above brokerage houses and reports thereon; and preparation of questionnaire for the New York Stock Exchange, also Federal and State taxes.

Providence-Biltmore Hotel, Providence, R. I.
Deschler Hotel, Columbus, Ohio
Laural House, Lakewood, N. J.
Secor Hotel, Toledo, Ohio
Lakewood Country Club, Lakewood, N. J.

Installation of entire department and financial systems. Am considered an authority on Hotel Accounting. My articles on this subject can be found in the library of the American Institute of Accountants, under the title of "Hotel Accounting" by Robert S. Rains.

[fol. 636] [Title omitted]

AFFIDAVIT OF JOHN H. BICKLEY

CITY OF WASHINGTON,
District of Columbia, ss:

John H. Bickley, being duly sworn on oath, deposes and says:

My legal residence is 1509 Sumac Drive, Shorewood, Madison, Wisconsin. I am Chief Accountant on the Telephone Investigation now being conducted by the Federal Communications Commission, pursuant to Public Resolution No. 8, 74th Session of Congress.

I was graduated from the University of Pennsylvania, in June, 1915, with the degree of Bachelor of Science in Economics.

From September, 1915, until June, 1924, with the exception of one year, I was Instructor, Assistant Professor, and Associate Professor in charge of Accounting instruction at Lehigh University, Bethlehem, Pennsylvania. I have conducted courses in Corporation Finance and Investments, as well as in different branches of Accounting.

In August, 1924, I became a senior accountant with the Public Service Commission of Pennsylvania. This position was held until October, 1925. At the latter date, I became [fol. 637] Chief Auditor of the Public Service Commission of Maryland by competitive examination. This position was held until December 31, 1926, when I became associated with the public accounting firm of Alonzo Lee Miles & Co., of Baltimore, Maryland. In May, 1928, I was engaged by

the Federal Trade Commission, in Washington, D. C., as a Public Utility Expert to assist in organizing and directing an investigation being made by that Commission of electric and gas utilities, their holding and associated management, engineering, construction and financing companies. This position was held until May, 1931, when I was appointed Chief of the Department of Accounts and Finance of the Public Service Commission of Wisconsin. Since April, 1935, I have been on leave of absence from the Public Service Commission of Wisconsin for the purpose of serving in my present capacity as Chief Accountant of the Telephone Investigation being conducted by the Federal Communications Commission.

During the course of my experience with public service commissions, I have been engaged on various cases involving the rates, practices, and finances of a number of public utilities, including telephone companies. There follows a list of some of the companies of which I have made investigations; also, the gross operating revenues of the companies, as of the year of the inquiry:

Name of Company	Gross Operating Revenues
Philadelphia Rapid Transit Company	$38,807,354
Equitable Gas Company	13,750,774
Consolidated Gas and Electric Company of Baltimore	21,459,698
Cumberland and Allegheny Gas Company	1,062,502
Wisconsin Power and Light Co.	8,342,198
Wisconsin Public Service Corp.	6,974,133
Wisconsin Gas and Electric Co.	5,541,712
Wisconsin Telephone Company	15,903,013
Milwaukee Gas Light Company	5,668,352

While with the Public Service Commission of Maryland I was engaged on the determination of the pre-license cost [fol. 638] of the Conowingo Hydro-electric Project of the Philadelphia Electric Company.

When in private practice, I was employed by the United Railways and Electric Company of Baltimore to audit the charges made against it by the Consolidated Gas and Electric Company of Baltimore under a cost-plus contract for the purchase of electric energy. This contract involved approximately $1,500,000 a year of purchase power by the Railway Company.

My first assignment as Public Utility Expert with the Federal Trade Commission was the preparation of a report form of two hundred twenty-five pages to be filled out by various companies. This was followed by the organizing of field work on accounting and financial investigations of electric and gas utilities, their holding and associated management, engineering, construction and financing companies. On all of this field work, I served in a consulting capacity and on a substantial part I exercised general supervison. There follows a list of companies on the investigation of which I gave more direct supervision. These are all holding companies. A substantial amount of work was performed on other companies, including several operating utilities.

Name of Company	Investments		Combined or Consolidated Gross Revenues
Electric Bond and Share Company	$799,709,025	(A)	$42,410,701
American Power and Light Company	239,603,883		80,222,149
Electric Power and Light Corporation	102,749,836		59,852,615
American Gas and Electric Company	104,047,191		68,021,531
Southeastern Power and Light Company	165,958,219		46,259,201
North American Company	132,700,581		147,779,869
New England Power Association	131,016,419		38,196,784
Middle West Utilities Company	206,817,296		162,337,274
Utilities Power and Light Corporation	72,946,707		51,453,619

(A) Gross operating revenue—not consolidated.

[fol. 639] It is estimated that the total consolidated fixed capital (at book value) controlled by the above holding companies was at least $4,500,000,000.

I am the author of several articles on public utility accounting and regulation.

I hold Certified Public Accountants' certificates from the States of Maryland and Wisconsin.

I was a member of the Committee on Statistics and Accounts of Public Utilities, of the National Association of Railroad Commissioners, from sometime in 1933 until November, 1935, and was Chairman of said Committee from January, 1934, until November, 1935. I was a member of the Special Committee on Telephone Depreciation of the same Association from January, 1934, until November, 1934.

I have examined and am familiar with the "Uniform system of Accounts for Telephone Companies, Issue of June 19, 1935, Effective January 1, 1936" (hereinafter sometimes referred to as "Revised System of Accounts"), prescribed by the Federal Communications Commission (hereinafter sometimes referred to as "Commission"). I have examined and am familiar with the "Uniform System of Accounts for Telephone Companies, Effective January 1, 1933" (hereinafter sometimes referred to as "Effective System of Accounts"), prescribed by the Interstate Commerce Commission. I have examined and am familiar with the "Uniform System of Accounts for Telephone Companies, First Issue, Effective January 1, 1913" (hereinafter sometimes referred to as "1913 System of Accounts"), prescribed by the Interstate Commerce Commission.

I have read the Bill of Complaint of American Telephone and Telegraph Company, et al, in this suit. I have read the Bill of Complaint of Ohio Associated Telephone Company, et al, in this suit.

[fol. 640] Part I. General Reply

I have read the affidavit of Roy B. Kester, John T. Madden, Charles A. Heiss and B. F. Young, all verified December 6, 1935, and the affidavit of Andrew Sangster, verified December 5, 1935.

All of the above-mentioned affiants, except B. F. Young, make certain accounting criticisms of certain portions of the Revised System of Accounts. In substance, these criticisms are directed toward the following:

1. That the definition of "cost", as applied to "original cost" of telephone plant means the cost of such plant when first dedicated to public use.

2. The requirement that when a going telephone plant is purchased, the accounts of the purchasing company must

record not only the cost to that company but also the original cost of the plant acquired.

3. The requirement that the investment in telephone plant must be classified as (a) plant in service, (b) plant under construction, (c) property held for future telephone use, and (d) as any difference between cost to the accounting company of telephone plant acquired by purchase and the original cost of such plant less certain reserves and other amounts.

4. That the Commission might require the writing off to surplus of all or a part of any difference between cost to the accounting company of telephone plant acquired by purchase and the original cost of such plant less certain reserves and other items.

[fol. 641] 6. That telephone companies will not be permitted to recover through expenses the entire depreciable investment in telephone plant, particularly that part of the investment which is in excess of the original cost of plant acquired by purchase, less certain reserves and other items applicable to the plant.

8. The requirement that all charges to the accounts for telephone plant, incomes, operating revenues, and operating expenses shall be "just and reasonable" and that any payments in excess of just and reasonable amounts shall be charged against income.

9. That telephone companies will incur additional expenses in setting up and keeping their accounts in conformity with the Revised System of Accounts.

[fol. 642] 1. Definition of Original Cost

A. The affiants on behalf of American Telephone and Telegraph Company, et al., generally characterize the definition as "unique" and "unusual". In the preparation of any set of rules or regulations it is essential to define certain key words. These definitions must be determined by the subject matter to which they relate. If this subject matter is proper and reasonable no justifiable criticism may be made of the definition which describes it.

B. Accounting authorities recognize that there are different kinds of costs. Each kind must be defined. It is

obviously necessary to give the meaning of each kind of cost through definition or otherwise. The Commission has found it necessary to distinguish between original cost and actual investment. It was, therefore, necessary to define what is meant by original cost. The definition given by the Commission is neither unique nor unusual. Different kinds of cost are considered in the regulation of public utilities. Some of these are "investment cost", "original cost", "historical cost", "current reproduction cost", and "reproduction cost at average prices". Regulatory commissions and the highest courts have used the term "original cost" for years in connection with regulation of public utility rates and other matters. The meaning of "original cost" as used in opinions and decisions of courts and commissions is in accord with the meaning given to the term by the Commission. Accountants, engineers, and lawyers engaged in public utility matters use the term repeatedly. Inasmuch as the term appears in the Revised System of Accounts it is necessary to define the sense in which it is used. The meaning given is the common and usual definition in public utility regulation.

2. The Recording of Both Cost to Company and Original Cost

A. The affiants on behalf of the American Telephone and [fol. 643] Telegraph Company, et al., appear to labor under the misapprehension that the Revised System of Accounts does not require the recording of actual investment in telephone plant and that it limits to original cost the amount recorded for telephone plant purchased. This is contrary to the definite requirements of the accounting system. The system specifically provides that the accounts for telephone plant shall record actual investment in all property. No choice in this respect is permitted and accounts kept on any other basis would be in violation of the prescribed rules. The Revised System of Accounts provides, further, that the accounts shall be so kept as to record, also, the original cost of telephone plant. For the preponderant part of telephone plant there will be no difference between original cost and actual investment. But in those instances in which differences exist, they will be shown. In every case, however, actual investment will be recorded.

B. It is my opinion that the requirements of the Revised System of Accounts for reporting both original cost and actual investment is reasonable and necessary and that it will provide valuable information for the public, investors, the management, regulatory bodies, taxing authorities and courts. The credit position of telephone companies is dependent largely upon the rates which they may charge for services rendered. In the determination of reasonable rates consideration must be given to the value of property used in telephone service and a fair return on such value. The value of telephone plant for rate-making purposes is determined by (a) the original cost, (b) the reproduction cost, and (c) such other matters as may be relevant.

C. The original cost of property existing at a given time is a constant and unvarying amount. It does not change [fol. 644] with the incidents of ownership. It is the same today, with respect to a certain piece of property, as it was ten years ago or as it would be ten years hence. On the other hand, reproduction cost is a varying amount, changing with variations in price levels and construction conditions. Insofar as cost to the owner of telephone plant might be a factor in the determination of value for rate-making purposes, this, too, may be a shifting amount. Through successive changes in ownership, the cost to the various owners may rise and fall and be different from the fixed amount of original cost and the varying amount of reproduction cost. The Commission has taken cognizance of these facts and has prescribed that the original cost of plant, the only unchanging element in the determination of value, shall be kept intact regardless of changes in ownership, the shifting of price levels, and changes in construction conditions.

D. It is my opinion that the furnishing of such information will be of value to all persons and official bodies interested in the earnings and financial condition of telephone companies. No harm can be done by the keeping of accounts in conformity with the needs of an informed public, investors, management, taxing agencies, regulatory commissions, and courts. It must be emphasized that the Revised System of Accounts requires the keeping of both actual cost to the accounting company and original cost.

E. The theory that accounting records should report by separate accounts (a) original cost, and (b) cost to the accounting company of property acquired by purchase is not "unusual" or "unique". It is found in the 1913 System of Accounts, the Effective System of Accounts, in the various classifications of accounts adopted by the National [fol. 645] Association of Railroad and Utilities Commissioners, and the accounting systems of all State commissions with which I am familiar. The account "Franchises" in all these systems provides that the amount included therein shall not exceed the amount originally paid to the government by the original grantee. If a franchise is purchased by one company from another, the purchasing company is subject to the same limitation. The same account provides, further, that any excess paid by the purchasing company over the amount paid to the government by the original grantee, shall be included in another account, generally designated "Miscellaneous Intangible Capital." Although the words "original cost" are not employed, except in the Effective System of Accounts, it is evident that such is the meaning of the franchises account.

F. It is significant to note, in connection with franchises, that the Effective System of Accounts refers to both "cost" and "original cost." Account 202, Franchises, in that system says that it shall include "also the original cost of franchises acquired by assignment." Inasmuch as that system of accounts generally refers only to "cost", in such matters, it would appear that a distinction is made between original cost and cost to the accounting company. Such a conclusion would be supported by the provisions of the preceding system, that effective from January 1, 1913 until December 31, 1932, which provided: "If any such franchise is acquired by assignment, the charge to this account in respect thereof should not exceed the amount actually paid therefor by the company to its assignor, nor should it exceed the amount actually paid the government." (Account 202, Franchises.)

[fol. 646] G. It may be noted, further, with respect to franchises, that Kester, an affiant for plaintiffs in this suit, comments with favor upon the same provision contained in a system of accounts for gas utilities prescribed by the

Public Service Commission of New York. In this connection he says:

Such careful regulations as to the content of intangible asset accounts are not always nor everywhere imposed at the present time. It is not putting the case too strongly to say that the reader of a balance sheet containing items about which practice is not standardized should always be on his guard to assure himself as to the content of such items in order to establish the legitimacy of their use and value. (R. B. Kester, Advance Accounting, Third Revised Edition, page 383.)

H. The account for franchises in the other systems of accounts, referred to above, places an amount not exceeding original cost in the franchises account and any excess of cost to the owning company in another intangible fixed capital account. Both are included in investment in fixed capital on the balance sheet in one account. I am of the opinion, however, that it would not be unsound to divide this balance sheet account into two parts in the same manner as that prescribed in the Revised System of Accounts. Such divisions of investment in fixed capital are not unusual. A division is contained in the 1913 System of Accounts, as follows:

Account 100, Fixed Capital Installed Prior to January 1, 1913.
Account 101, Fixed Capital Installed Since January 1, 1913.
Account 104, Construction Work in Progress.

3. Classification of Investment in Telephone Plant

A. The Revised System of Accounts provides four balance sheet accounts for investment in telephone plant. [fol. 647] These are:

100.1, Telephone plant in service.
100.2, Telephone plant under construction.
100.3, Property held for future telephone use.
100.4, Telephone plant acquisition adjustment.

Affiants on behalf of American Telephone and Telegraph Company, et al., generally criticize the above classification on the grounds that (a) it will be difficult to make, (b) dis-

agreements will arise, (c) that it may be misleading, and (d) additional expense will be incurred.

(a) It is my opinion that no more difficulty will be experienced in classifying investment in telephone plant in the manner prescribed than will be encountered on various other matters contained in any system of accounts. It is my further opinion that the provisions of the Revised System of Accounts are reasonably clear. A careful reading of the affidavits filed by affiants in behalf of plaintiffs leads me to the conclusion that they entertain misconceptions of the purposes and meaning of the classification of investment in telephone plant. They generally cite as one difficulty that of distinguishing between plant in service (account 100.1) and plant held for future telephone use (account 100.3). They give as an illustration the recording of spare plant, with particular reference to the pairs of wire in a cable when some pairs may be in use and others are not in use. It is my understanding that such cable will be included in the account for telephone plant in service (account 100.1). The provisions of the accounting system are reasonably clear on such matters. In any event, the Revised System of Accounts makes specific provision for the removal of such doubts if, and when, they arise. Instruction 9, page 8, [fol. 648] provides for the submission of questions to the Commission for interpretation, in this language: "To the end that uniformity of accounting may be maintained, the company shall submit all questions of doubtful interpretation of the prescribed accounting to this Commission for consideration and decision." A similar instruction is found in any systems of accounts for public utilities, and in my opinion, it is desired and necessary in order that the uniformity which is sought will be attained. The questions raised by affiants for plaintiffs can be disposed of through interpretations by the Commission. The universal experience under systems of accounts for public utilities is that such interpretations are necessary. The 1913 System of Accounts required numerous interpretations, and the Effective System of Accounts has called for them. In my opinion it is unfair and unreasonable to attack a set of rules and regulations because interpretations may be required. The most perfect statute may call for interpretation and the most perfect system of accounts will not be free of this need.

(b) In answer to the expressed fear that disagreements will arise in connection with the classification of telephone plant investment, it may be said that disagreements arise frequently among accountants, as well as among members of other professional groups in interpretations of matters with which they are familiar. Should conflict of views occur in connection with the classification of investment in telephone plant, such discord may be settled by companies referring disputed matters to the Commission for consideration and decision.

(c) It is my opinion that, instead of being misleading, the prescribed classification of investment in telephone plant will be a helpful guide to all parties interested and [fol. 649] concerned in understanding the financial condition of a telephone company. It can be misleading to anyone not familiar with the subject matter. This, however, is not peculiar to the Revised System of Accounts. The investing public has relied for years upon published balance sheets and income statements of corporations. In many cases, if investors or others were misled, it was because of their failure to understand the subject matter of the statements. I believe that the accounts of all corporations, and the published reports based upon those accounts, should be so kept and so stated as to be of greatest possible use and value to all interested parties. I have advocated for years the keeping of accounting records and the publishing of reports that will serve these ends in the most complete and informative manner. In my opinion, the Revised System of Accounts will serve to make available necessary and useful information for the guidance of all interested parties and that it marks a forward step in this direction.

(d) B. F. Young, in his affidavit for American Telephone and Telegraph Company, et al., makes estimates of additional cost that would be incurred by New York Telephone Company in setting up and keeping its accounts in conformity with the required classification of telephone plant investment. In the preparation of his estimates, he has assumed requirements which, in my opinion, do not obtain. To the extent that his studies are based upon these assumed requirements, they are inaccurate. A system which requires more complete, necessary and useful information

may entail some additional cost. An accounting system should be set up in accordance with the needs to be served, and any system which fails to recognize reasonable and [fol. 650] proper needs will fail in its purpose. It is my opinion that any additional work in connection with the prescribed classification of investment in telephone plant is justified by the additional necessary and useful information which it will make available.

4. The Writing Off of Telephone Plant Acquisition Adjustment

In the affidavits of affiants for American Telephone and Telegraph Company, et al., the assumption is generally made that telephone companies will be required to write off against surplus any amount included in account 100.4, Telephone Plant Acquisition Adjustment, for the excess of cost to the accounting company of telephone plant acquired by purchase over the original cost of such plant less certain reserves and other items. They assume further that no amount in account 100.4 could properly be charged off as an expense.

A. In my opinion both of the foregoing assumptions are unwarranted and unsupported by the wording of the Revised System of Accounts. Account 100.4 merely provides that the amount included therein with respect to each acquisition of plant "shall be disposed of, written off, or provision shall be made for the amortization thereof, in such manner as the Commission may direct." I do not understand this to mean that the Commission shall direct telephone companies to write off all of the adjustment account by deductions from surplus. It is my opinion that the Commission has given recognition to the various factors which may account for the amount in the adjustment account and has provided for the individual consideration thereof in the light of the facts as they are determined.

B. It is my knowledge, based upon experience in analyzing the transactions of public utilities, that an excess of cost to an accounting company over the original cost of [fols. 651 & 652] property purchased is due to a variety of elements, such as, (a) payments made by purchasing companies for going value and water power value, (b) differences in price levels, (c) a capitalization of advantages ex-

pected to be derived through the merger of plants and the integration of systems, and (d) payment made by the purchasing company for an opportunity to enter what it considers to be profitable territory.

C. It is my opinion that the interests of utilities and their patrons are best served by a consideration by the Commission of the facts in each case. There is no mandate on telephone companies to write off to surplus all or a part of the amount included in account 100.4, Telephone Plant Acquisition Adjustment. There is no foundation for the fear that the Commission will order the writing off to surplus of all amounts included by telephone companies in this account. If such concern exists in the minds of the responsible officers of telephone companies, this may be dispelled by requests to the Commission for interpretation of the account as provided in Instruction 9, at page 8.

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[fol. 653] 6. Recovery of Depreciable Investment Through Expense Charges

Affiants for American Telephone and Telegraph Company, et al., misconstrue the requirements with respect to account 100.4, Telephone Plant Acquisition Adjustment, to mean that no part thereof may be charged off as an operating expense. This contention is not supported by any statement in the system. The accounting rules are so designed as to require telephone companies to report as expenses the things which are expenses. The application of account 100.4 will doubtless be such as to require the inclusion in operating expenses of amounts which should be recovered in this manner. The misapprehension by affiants for plaintiffs appears to be based upon their erroneous assumption in connection with and their interpretation of the Revised System of Accounts. The proper solution of this question may be had through an interpretation by the Commission. I would be unwilling to prejudge a case by assuming that such interpretation would violate sound accounting principles.

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[fol. 654] 8. Just and Reasonable Charges

A. Affiants on behalf of American Telephone and Telegraph Company, et al., take exception to Instruction 2-B.1 in the Revised System of Accounts, which provides as follows:

All charges to the accounts prescribed in this classification for telephone plant, income, operating revenues, and operating expenses, shall be just and reasonable and new payments made by the company in excess of such just and reasonable charges shall be included in account 323, "Miscellaneous Income Charges".

[fol. 655] B. This requirement is intended, in my opinion, to separate unjust and unreasonable charges from just and reasonable charges. It might well be assumed that telephone companies will endeavor to avoid unjust and unreasonable payments. Nevertheless it is equally incumbent upon a regulatory commission to establish such rules as will at least separate unjust and unreasonable payments from those which are proper. If it is to be assumed that all payments, regardless of their reasonableness, are to find their way into the plant accounts and the operating expenses of telephone companies and that these amounts are to enter into a determination of reasonable rates, then a burden is placed upon telephone patrons. If such rules are not written into a system of accounts for companies engaged in a public service, a regulatory commission, in my opinion, would be deprived of essential information for effective regulation. The interest of investors is at stake in such matters. If the management makes unjust and unreasonable expenditures, this fact should be clearly indicated. The Commission has set up the means of making this information available to those whose money is invested in the enterprise.

C. Complaint is made that there will be difficulty in distinguishing unjust and unreasonable expenditures. This may be true in isolated cases but generally little difficulty will be encountered. If disagreement arises as to whether or not any improper expenditure was made, the facts may [fol. 656] be submitted to the Commission for decision. It is to be borne in mind, however, that such decision, insofar

as the Revised System of Accounts is concerned, will be to determine whether all or a part of the payment is to be included in the Accounts for telephone plant and operating expenses (the accounts which will usually be involved) or in account 323, Miscellaneous Income Charges. That is, insofar as the accounting rules are concerned, the question concerns the account or accounts to be charged for the payment.

D. The requirement of "reasonable" costs is not unusual in systems of accounts for public utilities. Construction costs may include charges for interest during construction but only "reasonable" amounts may be so charged. Instruction 22 (B) (10) (a), of the Effective System of Accounts provides:

Reasonable amounts for interest during the construction period * * * shall be charged to the telephone plant accounts. * * *

What is a "reasonable" amount of interest? What is a "reasonable" interest charge to construction? These questions have been debated for years by persons interested in public utility accounting and regulation. Sharp conflict and considerable difference of opinion exists. There is no "uniformity of judgment." Accountants are frequently required to investigate individual transactions or jobs to ascertain whether or not interest should be charged and the reasonableness of the amount. Substantial difficulty is experienced in many cases. These circumstances, however, do not impair the usefulness of the word and the restrictions which it is intended to impose.

9. Additional Expenses of Setting up and Keeping Accounts

A. My opinion on this matter is set forth under paragraph 3-A (d), above.

[fol. 657] Part II. Reply to Kester

Inasmuch as the affidavit of Roy B. Kester sets forth substantially the same objections and opinions as those contained in the affidavits of Charles A. Heiss, John T. Madden, and Andrew Sangster, detailed comments on and replies to Kester's affidavit are made hereinafter.

1. At the bottom of page 3, Kester says: "The above system of accounts provides two definitions of "Cost" as follows:" The Revised System of Accounts defines several kinds of cost, such as "Book cost" (Instruction 3-E), "Cost of removal" (Instruction 3-H), and "Original cost" (Instruction 3-S.1). Each kind of cost has reference to certain conditions and subject matter and each is defined for the purpose of establishing uniform terminology and usage in connection with particular conditions. This is essential for accuracy, clarity, and uniformity. In every field of thought such definitions are used. In accounting, there are various kinds of cost and various kinds of other items, such as surplus, reserves, capital stock, etc. In each instance, the kind of cost, surplus, or reserve must be defined. Kester, in his published writings, refers to different kinds of cost.

2. At page 4, third paragraph, Kester characterizes the definition of "cost" in reference to "original cost" as "unique." He does not say that it is an inaccurate or unreasonable definition from an accounting or any other viewpoint. He continues, same paragraph, that original cost, as defined by the Commission, "brings into the accounting records a cost basis which is not *current cost* and is therefore not the cost of the reporting company." (Italics are supplied.) He does not make clear what he means by "current cost," whether it means cost at any given time, cost of current reproduction, a cost which is current as distinguished from a prior cost, or cost at the [fol. 658] time of a transaction. "Current cost" might be different from "cost of the reporting company," depending upon the definition of current cost. Furthermore, Kester, in his published writings, recognizes that an asset may properly be carried in the accounts of the owner at an amount different from cost to the owner.

3. At page 4, fourth paragraph, Kester says: "The *records* of an individual concern must show what its own costs are; never those of a competitor, nor what its own costs might have been had other conditions prevailed or other decisions have been made than those which were made. In other words, the *record* of each concern must provide an accurate history of what actually took place in the con-

cern." (Italics are supplied.) I agree with this statement. The Revised System of Accounts requires that the "records" of a telephone company show what its costs have been and do not permit the "record" of any company to show the costs of a "competitor" or what its costs would have been had other conditions prevailed. The system provides that the records of a company for its telephone plant must show what has taken place with respect to its telephone plant in a most informative and accurate manner.

4. At page 5, first paragraph, Kester says: "The above system of accounts sets up three property investment accounts, 100.1, 100.2 and 100.3, * * *." This is in error. The revised system of accounts provides four accounts, 100.1, 100.2, 100.3, and 100.4, for investment in telephone property and certain other accounts which are inseparately related to said accounts.

5. At page 5, second paragraph, Kester says: "In the case of purchased property, none of these accounts will show the actual cost of the accounting company (its actual investment), unless by coincidence the purchaser has paid the seller exactly what the property cost the original dedi- [fol. 659] cator." This is in error. In the event the present owner of telephone plant has purchased plant at an amount equal to the original cost to the original dedicator (the coincidence to which Kester refers), neither the three telephone investment accounts cited by Kester, nor the four accounts which are in fact provided, will report the "actual cost to the accounting company (its actual investment)" of such plant. Under the Effective System of Accounts, the telephone investment acounts, when considered alone, do not record the actual investment by the accounting company in purchased property. The telephone investment accounts of plaintiff companies do not now record their actual investment in purchased property, certainly to the extent that plant has been purchased since January 1, 1933. Under both the Revised System of Accounts and the Effective System of Accounts, the actual cost to the accounting company is determined only by considering several accounts.

6. At page 6, first paragraph, Kester says: "No provision is made for the expense of depreciation with respect

to the portion of the investment recorded in Account 100.4." The Revised System of Accounts provides that amounts included in account 100.4, Telephone Plant Acquisition Adjustment, "shall be disposed of, written off, or provision shall be made for the amortization thereof in such manner as the Commission may direct." There is no provision in the system by which all or a part of an amount included in account 100.4 would not be written off as an expense. The system does not, and should not, make specific reference to every detailed transaction, operation, occurrence, or condition to be expressed in the accounts of telephone companies. To do so, would require volumes of printed matter and would exceed the requirements of a system of accounts. In my opinion, the treatment accorded amounts included in account 100.4 should depend upon the facts which give rise to such amounts.

7. At page 6, second paragraph, it is said: "The amounts [fol. 660] in Account 100.4 are not distributed among the plant accounts, i. e., 'buildings,' 'pole lines,' etc. (Accounts 201-277, pages 47-61.)" Under the 1913 System of Accounts, in effect until January 1, 1933, the accounts for buildings, pole lines, etc., did not record the total investment in such classes of plant. All elements of cost were not included in the plant to which they were applicable. Furthermore, the Commission, in its administration of account 100.4, might direct that all or a part of an amount included therein be classified as amounts applicable to buildings, pole lines, etc., according to the facts in the case. There is nothing in the system which prohibits telephone companies from making this classification. It may not be assumed, however, that all amounts included in account 100.4 can or should be identified with various classes of plant. For example, if the account includes an amount for going value, the propriety of distributing this intangible to the tangible classes of plant is very doubtful. In fact, Kester, in his published writings, says that "goodwill" should be reported separately on the balance-sheet.

8. At page 6, third paragraph, it is said that, with respect to purchased plant, accounts 100.1, 100.2, and 100.3 will not show the actual cost to the accounting company. This is true in part only but Kester improperly dissociates these accounts from other related accounts. Account 100.2,

Telephone Plant under Construction, is treated in the same manner in both the Effective System of Accounts and the Revised System of Accounts with respect to purchased plants. Under both of these systems and under the 1913 System of Accounts, the telephone plant accounts do not in all cases include or record the cost to the accounting company.

9. At page 6, fourth paragraph, it is said that the amount in acount 100.4, Telephone Plant Acquisition Adjustment, [fol. 661] "*must* be extinguished." This is an unwarranted assumption and fails to express the provisions of the Revised System of Accounts. The system provides that the amount in account 100.4 "shall be disposed of, written off, or provision shall be made for the amortization thereof in such manner as the Commission may direct."

There is no mandate on the Commission to order the immediate or ultimate extinguishment of an amount in the account with respect to a particular purchase of plant. In any event, Kester's opinion is based upon his interpretation. It must be presumed that the account will be interpreted by the Commission if such interpretation becomes necessary. The Revised System of Accounts makes adequate provision for interpretations and, if doubt exists in the minds of the responsible accounting officers of plaintiffs, they may freely obtain clarification. Every system of accounts has required interpretation. Numerous interpretations were made by the Interstate Commerce Commission of its 1913 System of Accounts. There is every probability that the Effective System of Accounts will call for interpretations. The Revised System of Accounts has the necessary flexibility to meet the exigencies of particular cases which Kester does not recognize in his affidavit. If he has given consideration to all the elements and conditions which occasion a difference between the cost of constructing tangible property and the price paid for a going business, he does not refer to them. Nevertheless, in his published writings, he advocates the exclusion of such an intangible as goodwill from the accounts for plant investment.

10. Kester continues, page 6, fourth paragraph, "The company is not allowed to recover, through depreciation charges, its own investment in property which is being used up, * * *." Telephone companies are not allowed,

under the Effective System of Accounts and were not al-
[fol. 662] lowed under the 1913 System of Accounts to recover, through depreciation charges, their entire investment in property under certain conditions.

11. At page 7, Kester summarizes his objections to the prescribed accounting, in the Revised System of Accounts, for investment in telephone property. In the opinion of your affiant, Kester directs his criticism against a condition which does not exist. The system clearly requires that the accounts of telephone companies record the cost to them of telephone property purchased. Kester appears to completely ignore this requirement.

12. In his summary of objections, Kester makes at least one contradictory statement, to wit: "Sound accounting requires that the accounts of a company shall correctly record the transactions of that company and truly reflect its condition." (Paragraph (a), page 7.) Under a given set of circumstances it would be impossible for the accounts of a company to report these two conditions at one and the same time. Some transactions of a company may have been unfortunate, if not disastrous, and the true condition of the company would not be reflected by the accounts for these transactions.

13. After misconstruing the provisions of the Revised System of Accounts, Kester says (page 7, paragraph (c)): "Accounts kept on such a basis would be misleading to the public, to investors, to the company's management, to legislatures, to future regulatory bodies, to taxing authorities and to the courts. The system of accounts requires the accounts to be kept on this unsound basis." In my opinion, the Revised System of Accounts does not establish an unsound basis. The system provides accounting methods and produces accounting statements which are more enlightening, informative, and valuable to the public, investors, management, legislatures, regulatory bodies, taxing authorities and courts than the Effective System of Accounts or the
[fol. 663] 1913 System of Accounts. In connection with purchased plant, certain facts which have a direct bearing upon the profits of telephone companies are clearly set forth for the information and guidance of all interested parties. These are the facts against which Kester lodges his complaint.

14. Kester concludes that account 100.4, Telephone Plant Acquisition Adjustment, is a deferred charge against surplus (first sentence, page 8). This is contrary to fact and is an unwaranted assumption, based apparently upon an erroneous interpretation. The amount in account 100.4 is an asset, to be reported as such, as long as it continues to be an asset. Large amounts included in the plant accounts of plaintiff companies will cease to be assets in the near future. When they are no longer assets, they will be removed from the asset accounts. They will cease to be assets because of various circumstances. Certain present assets may be written off in whole or in part against surplus. Most items of telephone plant are mortal and provision is made for mortality. Under the Revised System of Accounts, the accounts will record the cost to a company of its property as long as the property exists.

15. In a sense, the preponderant part of plaintiff's investment in telephone plant is a deferred charge. Most of it is being, and will continue to be, charged off as an expense but some of it may be written off to surplus.

16. In paragraph (d), page 8, Kester unwarrantedly assumes that telephone companies will be required to record losses which have not occurred.

17. At the top of page 9, Kester says that the effect of the prescribed account for account 100.4, "is that the accounts will not record the impairment of the company's own investment, but will record, so far as purchased property is concerned, a depreciation expense which is related only [fol. 664] to the investment of some one else." This, again, is an improper and unwarranted assumption and is prejudgment. Regulatory bodies, the Federal Communications Commission included, must be assumed to desire the recording by telephone companies of the impairment of investment. The entire body of accounting regulations which are being given more serious consideration today than perhaps ever before are predicated largely on this point of view. If such impairment is an expense of telephone companies in their rendering of telephone service, it doubtless will be treated as such an expense and the Revised System of Accounts makes adequate provision for this condition. On the other hand, not every loss, or impairment of capital, is an expense of rendering telephone service. To view a tele-

phone business otherwise, would free investors from the risks inherent in every business.

18. At page 10, first paragraph, Kester objects to the use of the word "imminent" in account 100.3, Property Held for Future Telephone Use. He criticizes the language of the account because accountants might disagree as to what property is to be included therein. Your affiant has had experience with two systems of accounts (those in general use) for telephone companies and has learned that accountants are not always in accord in their interpretations of these systems. This is not peculiar to accountants or to accounting systems. If there is doubt in the minds of the responsible accounting authorities of telephone companies as to whether or not a certain piece of property is to be included in account 100.3, such doubt may be removed by interpretation by the Commission. Similar doubts have been disposed of in the past by this procedure and will have to be met in the future. In the opinion of your affiant, the Commission merely recognizes that a piece of property, such as a parcel of land, might be in use in telephone service; that it might have been acquired for such use ultimately, [fol. 665] but not be used at all, currently; or that it might be used for non-telephone purposes. The classification of investment established by the Commission is in accord with facts and violates no principle of accounting.

19. Kester alleges, further, at page 10, second paragraph, that "Accountants will also experience great difficulty in determining what property is 'used' in telephone service—Account 100.1—as distinguished from that 'held for imminent use'—Account 100.3." The account continues: "under a definite plan for such use." The Effective System of Accounts provides that Account 100, Telephone Plant, shall include property "used" or held "under a definite plan" for telephone service. The same objection can be raised to the language, "definite plan." When is a plan "definite"? Both accountants and engineers may disagree on this, but a system of accounts is not unreasonable, unsound or invalid because such disagreement arises. By such standards the existence of all moot questions evidence unsound and unreasonable conditions. In any event, such doubts may be

removed by the Commission through interpretation when called for.

20. The possibility that accountants will experience difficulty in interpreting a system will present no unique or unusual condition. In my opinion, no system of accounts and no text book on accounting will be written that will not present difficulties and disagreement in interpretation. Perfection in the expression of thought is desirable, but, unfortunately, is rarely, if ever, attained. It is possible that Professor Kester has had occasion to interpret his writings to persons versed in accounting theory and practice. It would be most unfortunate if his works were characterized as unsound by reason of the possibility, if not the fact, that interpretations were necessary.

21. In the Revised System of Accounts, the Commission has undertaken to segregate property not in use in tele- [fols. 666-668] phone service from property which is in use. In the opinion of your affiant, this is reasonable, necessary and useful segregation for the guidance of the public, investors, management, regulatory commissions, taxing authorities, and courts and is in harmony with sound accounting principles.

. . . . . .

[fol. 669] 27. Beginning the bottom of page 14, Kester criticizes the requirement of "just and reasonable" charges because of the element of judgment involved. It must be pointed out that judgment plays a considerable part in recording many things in the accounts. This is particularly true of such matters as depreciation, the apportionment of expenditures to construction and operations, allocations to various accounts, and the capitalization of interest and general expenses. (For further reply, see section 8 of Part I.)

[fols. 670-673] Part III

Reply to Complaint of Ohio Associated Telephone Company, et al., and Affidavit of Harold V. Bozell

A. I have read the bill of complaint of Ohio Associated Telephone Company, et al., and the affidavit of Harold V. Bozell, verified December 6, 1935.

B. I find that the complaints of above mentioned plaintiffs and the contentions of Bozell are similar in substance to the complaint of American Telephone and Telegraph Company, et al., and the affidavits of affiants in behalf of the latter plaintiffs.

. . . . . .

[fol. 674] It is my considered judgment that the provisions of the Revised System of Accounts complained of are all designed to serve, and that they will serve, the interests of investors, management, telephone patrons and governmental bodies in a most essential, practical and useful way.

John H. Bickley.

Subscribed and sworn to before me this 11th day of December, 1935. Rosel H. Hyde, Notary Public. My commission expires May 19, 1936.

[fol. 675] [Title omitted]

AFFIDAVIT OF ASEL R. COLBERT

DISTRICT OF COLUMBIA,
City of Washington, ss:

Asel R. Colbert, being duly sworn on oath, deposes and says:

I reside at 2518 North 60th Street, Milwaukee, Wisconsin. I am Acting Director of the Department of Accounts and Finance of the Public Service Commission of Wisconsin. I have been engaged in this capacity since May, 1935. As Acting Director of this Department, I am in charge of the preparation of systems of accounts for utilities in the State of Wisconsin; of accounting investigations of these utilities for rate making and other purposes; of reviewing applications of utilities for the issuance of securities and making recommendations thereon to the Commission, and of other matters concerned with the regulation of utility accounting under the public utility statutes of Wisconsin.

From September, 1931, until May, 1935, I was employed by the Public Service Commission of Wisconsin as a Spe-

cial Public Utility Investigator. In this capacity I was in direct charge of various accounting investigations of utility companies operating in Wisconsin. As a part of certain of these investigations, analyses were made to determine the original cost of utility property.

From July, 1928, to September, 1931, I was employed by the Federal Trade Commission, Washington, D. C., as an accounting examiner engaged in investigating the accounts and records of public utility holding companies and [fol. 676] their subsidiary operating, construction and servicing companies. During the course of my employment with the Federal Trade Commission I worked on the accounts and records of Electric Bond and Share Company, National Power and Light Company, Middle West Utilities Company, North West Utilities Company, United Public Service Corporation, United Public Utilities Company, Central Illinois Public Service Company, Appalachian Electric Power Company, and Mississippi Valley Utilities Investment Company, as well as other smaller companies. On all of these except the Electric Bond and Share Company and Appalachian Electric Power Company I was in charge of the field investigation with a force of senior and junior accountants under my supervision.

From July, 1927, until July, 1928, I was employed as an accountant by Martin W. Cookerow (deceased), attorney and certified public accountant, associated with the law offices of C. Bascom Slemp, Washington, D. C.

From 1923 to July, 1927, I was employed in an accounting capacity by the Chicago Heights Terminal Transfer Railroad Company, Chicago Heights, Illinois.

From 1921 to 1923 I was employed by Martin W. Cookerow (deceased), attorney and certified public accountant of Washington, D. C.

I have read the Bill of Complaint of American Telephone and Telegraph Company, et al. in this suit. I have read the Bill of Complaint of Ohio Associated Telephone Company, et al. in this suit.

I have read the affidavits of Andrew Sangster, John T. Madden, Roy B. Kester, B. F. Young, and Charles A. Heiss, filed on behalf of the plaintiffs in this case.

I am familiar with the Uniform System of Accounts for Telephone Companies prescribed by the Federal Communications Commission under the provisions of the Communi-

cations Act of 1934, Issue of June 19, 1935, effective January 1, 1936.

1. Provisions with Respect to Cost of Property

(A) The uniform system of accounts prescribed by the Federal Communications Commission, effective January 1, 1936, provides that two material facts shall be shown with respect to the company's investment in telephone property. It is provided that the cost to the accounting company shall be recorded in its accounts, and that there shall [fol. 677] be shown likewise the original cost of the property at the time it was first dedicated to public use. With respect to the first requirement, namely, that of showing the cost to the accounting company of its property, the system of accounts conforms to a long established accounting practice of recording the investment in property and plant at cost. Plaintiffs claim at page 9 of the Bill of Complaint that the system of accounts will require that the plaintiffs, as of January 1, 1936, "restate their then existing property investment accounts by eliminating therefrom the recorded cost or investment of plaintiffs in property theretofore acquired by them from another public utility, and substituting for such recorded cost or investment the amount (estimated if not known) which said property cost some former owner at the date of first dedication to public use."

(B) It is true that the system of accounts will require a restatement of existing property investment accounts. However, this restatement is not accomplished by "eliminating therefrom the recorded cost or investment" in property. The system of accounts provides that the cost of plaintiffs' investments shall be shown in their accounts. There is to be shown, also, the original cost of such investment, as defined in said system of accounts. The cost to the accounting utility or its investment in property, before consideration of depreciation reserves, amortization reserves and contributions for extensions, is shown by four investment accounts. These are:

Account 100.1—Telephone plant in service.
Account 100.2—Telephone plant under construction.
Account 100.3—Property held for future telephone use.
Account 100.4—Telephone plant acquisition adjustment.

All these accounts are carried under the term "Investments" in a balance sheet prepared in accordance with this system of accounts. (Page 25 of System of Accounts.) It will be noted, also, that the four accounts listed are identified by a subnumber under one main account number. This indicates that these accounts are related to one another. In fact, when they are considered together, there is shown the total gross investment in telephone plant before consideration of related reserves and contributions of telephone plant. The system of accounts has simply provided for classification of this investment. It is first classified as [fol. 678] between its original cost and the excess of cost to the accounting utility over the original cost. The original cost is further classified as between telephone plant in service, telephone plant under construction, and property held for future telephone use.

(C) At page 6, paragraph (c), of his affidavit Roy B. Kester states. "It is unsound and unheard of to keep a company's accounts neither on the basis of cost to it nor of value, but on the basis of the costs of someone else for which the accounting company has no responsibility." The system of accounts provides that the company record its property in its accounts on the basis of actual cost to the accounting company. There is also required by the system a division of such cost as between the original cost of the property and the excess of the cost to the accounting company over such original cost. This excess cost to the accounting company over original cost less related reserves and contributions of telephone plant, is recorded in the investment accounts of the company in account 100.4, Telephone Plant Acquisition Adjustment. Kester states in paragraph (c) at page 6 of his affidavit, that "it is true that so long as the 'difference' remains in the 'adjustment' account, it is technically listed as an asset of the company, but since its extinction is mandatory and may be immediate if the Commission so wills, it should not be regarded as an asset in anything but name." In my opinion this premise is not warranted. The telephone plant acquisition adjustment account is a part of the cost to the accounting company of its property and is so stated in the system of accounts. It is universally recognized that the cost of property should be recorded as an asset. This applies also to any portion of the cost. I believe that it is the intention

of the system of accounts that the telephone plant acquisition adjustment account be considered as a part of the assets of the company. This is reflected by the fact that the system of accounts includes the adjustment account as a part of the investment in property.

2. Telephone Plant Acquisition Adjustment

(a) It is provided, in the system of accounts at paragraphs (b) and (c) of the text relating to account 100.4, Telephone Plant Acquisition Adjustment, that,

[fol. 679] (B) "This account shall be subdivided according to the character of amounts contained therein. In addition to a copy of the journal entry recorded to open the account, the company shall file with the Commission statements showing the basis of the computation of amounts included therein. The detailed records supporting these statements shall be retained permanently by the company."

(C) "The amounts recorded in this account with respect to each property acquisition shall be disposed of, written off, or provision shall be made for the amortization thereof in such manner as this Commission may direct. (Note also Instructions 21.)"

(B) In my opinion these instructions considered together mean that when the accounting utility shall have determined the amounts includible in Account 100.4, Telephone Plant Acquisition Adjustment, it should submit full details concerning the same to the Commission and that thereupon the Commission will issue such order regarding the disposition of the amounts as is warranted by the facts in the case. This means that the amount might be permanently retained in the investment accounts, depreciated or amortized over the life of the property, or subject to such other disposition as might be appropriate for the items included in Account 100.4.

(C) The classification of accounts prescribed by the Public Service Commission of Wisconsin for electric utilities provides an account termed "Fixed Capital Purchase Adjustment" which is comparable to the telephone plant acquisition adjustment account contained in the Federal Communications Commission System of Accounts for Telephone Companies. In connection with the accounting work

necessary in determining the amounts to be included in such an account, I have found that the nature of items includible in the Fixed Capital Purchase Adjustment Account differ according to the facts in the various cases. In some cases, going value will be found to be the cause of the purchase adjustment; in other cases, water power value; in others, decline in the purchasing power of the dollar; and still other cases are found where the primary reason for the excess of the purchase price over the original cost is the elimination of a competitive situation, or the desire on the part of promoters to secure more properties to be refinanced or resold at profit to themselves. Under such conditions it is practically impossible to make a uniform rule with respect to the disposition of amounts includible in Account 100.4, Telephone Plant Acquisition Adjustment, which would be applicable in all cases. The facts must first be known. Appropriate directions may then be issued for the retention or the disposal of the account in accord-
[fol. 680] ance with the principles set forth in the system of accounts.

* * * * * * *

4. Property Includible in Property Held For Future Telephone Use

(A) At paragraph 10, page 15 of the Bill of Complaint, plaintiffs state that "the nature of plaintiffs' business is such that a portion of their property during periods of its life necessarily constitutes what is known as spare plant.
[fol. 681] Said system of accounts requires that such property be included in Account 100.3, 'Property Held for Future Telephone Use,' during such periods." I assume that what is meant by "spare plant" is plant in excess of immediate requirements. Cables, for example, may be installed with a capacity in excess of immediate requirements. This excess capacity may be termed spare plant.

(B) It is my opinion that when telephone plant is used it is to be included in Account 100.1, Telephone Plant in Service. The system of accounts states that "this account shall include the original cost (Note instruction 3-S. 1) of the company's property used in telephone service at the date of the balance sheet as classified under Accounts 201

to 277, inclusive (Note also instructions 3-AA, 20, and 21)." I interpret this to mean that if plant is used, regardless of how small the extent of use may be, it would be includible in Account 100.1, Telephone Plant in Service. In the System of Accounts for Electric Companies in use in Wisconsin, similar accounts for Property in Service and Property Held for Future Use are provided for. What is commonly known as spare plant, that is, plant that is used, but not to its full capacity, has always been considered properly chargeable to the Property in Service accounts.

(C) It is my opinion, further, that property includible in Account 100.3, Property Held for Future Telephone Use, would usually consist of property which had never been used in telephone service. Examples would be cases where land might be purchased for central office purposes considerably in advance of its requirement, or where conduit might be installed, but not used, even partially, for some time. I do not believe that the system of accounts intends, nor do I think it states, that spare plant or plant used only partially, is to be included in this account.

5. Just and Reasonable

(A) Instruction 2-B. 1 of the system of accounts provides that "all charges to the accounts prescribed in this classification for telephone plant, income, operating revenues, and operating expenses shall be just and reasonable and any payments by the company in excess of such just and reasonable charges shall be included in Account 323. 'Miscellaneous Income Charges.'"

[fol. 682] (B) At page 16 of the affidavit of John T. Madden it is stated that "any such requirement is unsound and contrary to correct accounting principles." The accounts of the public utility are of great importance in the regulation of rates. The cost of construction and the cost of operating expenses are important things for the consideration of regulatory bodies. A customary requirement is that the operating expenses considered should not be unjust nor unreasonable. It is, therefore, important that if unjust or unreasonable costs are incurred they should be segregated from just and reasonable charges. The requirement in the system of accounts that this be done

necessary in determining the amounts to be included in such an account, I have found that the nature of items includible in the Fixed Capital Purchase Adjustment Account differ according to the facts in the various cases. In some cases, going value will be found to be the cause of the purchase adjustment; in other cases, water power value; in others, decline in the purchasing power of the dollar; and still other cases are found where the primary reason for the excess of the purchase price over the original cost is the elimination of a competitive situation, or the desire on the part of promoters to secure more properties to be refinanced or resold at profit to themselves. Under such conditions it is practically impossible to make a uniform rule with respect to the disposition of amounts includible in Account 100.4, Telephone Plant Acquisition Adjustment, which would be applicable in all cases. The facts must first be known. Appropriate directions may then be issued for the retention or the disposal of the account in accord-
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* * * * * * *

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[fol. 681] Said system of accounts requires that such property be included in Account 100.3, 'Property Held for Future Telephone Use,' during such periods." I assume that what is meant by "spare plant" is plant in excess of immediate requirements. Cables, for example, may be installed with a capacity in excess of immediate requirements. This excess capacity may be termed spare plant.

(B) It is my opinion that when telephone plant is used it is to be included in Account 100.1, Telephone Plant in Service. The system of accounts states that "this account shall include the original cost (Note instruction 3-S. 1) of the company's property used in telephone service at the date of the balance sheet as classified under Accounts 201

to 277, inclusive (Note also instructions 3-AA, 20, and 21)." I interpret this to mean that if plant is used, regardless of how small the extent of use may be, it would be includible in Account 100.1, Telephone Plant in Service. In the System of Accounts for Electric Companies in use in Wisconsin, similar accounts for Property in Service and Property Held for Future Use are provided for. What is commonly known as spare plant, that is, plant that is used, but not to its full capacity, has always been considered properly chargeable to the Property in Service accounts.

(C) It is my opinion, further, that property includible in Account 100.3, Property Held for Future Telephone Use, would usually consist of property which had never been used in telephone service. Examples would be cases where land might be purchased for central office purposes considerably in advance of its requirement, or where conduit might be installed, but not used, even partially, for some time. I do not believe that the system of accounts intends, nor do I think it states, that spare plant or plant used only partially, is to be included in this account.

5. Just and Reasonable

(A) Instruction 2-B. 1 of the system of accounts provides that "all charges to the accounts prescribed in this classification for telephone plant, income, operating revenues, and operating expenses shall be just and reasonable and any payments by the company in excess of such just and reasonable charges shall be included in Account 323. 'Miscellaneous Income Charges.'"

[fol. 682] (B) At page 16 of the affidavit of John T. Madden it is stated that "any such requirement is unsound and contrary to correct accounting principles." The accounts of the public utility are of great importance in the regulation of rates. The cost of construction and the cost of operating expenses are important things for the consideration of regulatory bodies. A customary requirement is that the operating expenses considered should not be unjust nor unreasonable. It is, therefore, important that if unjust or unreasonable costs are incurred they should be segregated from just and reasonable charges. The requirement in the system of accounts that this be done

is an aid in the regulation of telephone companies. Furthermore, it imposes no hardship on the accounting officers of the company.

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[fols. 683 & 684] 7. Cost of Record Keeping

(A) At page 5 of his affidavit of December 6, 1935, B. F. Young estimates that "the cost to the New York Telephone Company of transferring property in and out of Account 100.1 as it became used or unused in telephone service, would be $1,177,700.00 per year, and that the cost for the first year, including the cost of establishing the segregation initially, would be $4,187,395.00." In making this estimate, it is stated in the affidavit at page 4 that "for the purpose of the study I assumed that when a telephone is taken out the pair of wires (whether in cable or otherwise) connecting that telephone with the central office is no longer used in telephone service and must therefore be transferred from Account 100.1 to Account 100.3."

(B) In my opinion, no such procedure is contemplated by the system of accounts. It would be an accounting absurdity to separate the cost of the pair of wires serving a particular customer from the rest of the cable and to transfer the cost of this pair of wires to Account 100.3 because the customer discontinues service.

(C) It appears reasonable that Mr. Young's estimate of cost is influenced considerably by his assumption with respect to transfers of property from Account 100.1 to 100.3. In my opinion, his assumptions are not in accord with the requirements of the system of accounts and therefore his estimate of cost of record keeping thereunder can not be correct.

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[fol. 685] 10. System Approved by National Association of Railroad and Utilities Commissioners

(A) The uniform system of accounts was approved by the National Association of Railroad and Utilities Commissioners at its convention in Nashville, Tennessee, held in October, 1935. The National Association recommended to the several state commissions represented in the Associa-

tion, which exercise jurisdiction over the accounts of telephone utilities, that they respectively adopt and prescribe the uniform system of accounts prescribed by the Federal Communications Commission, effective as of January 1, 1936.

[fol. 686] 11. System Prescribed by Public Service Commission of Wisconsin

(A) The uniform system of accounts for telephone companies prescribed by the Federal Communications Commission, effective January 1, 1936, has been adopted and prescribed by the Public Service Commission of Wisconsin. As Acting Director of the Department of Accounts and Finance, I reviewed the System of Accounts and recommended its adoption. I made such recommendations with the belief that said system of accounts conforms to recognized principles of accounting and is designed to give information essential to regulatory bodies concerned with the accounting of telephone utilities.

Asel R. Colbert.

Subscribed and sworn to before me this 11th day of December, 1935. Rosel H. Hyde, Notary Public. My Commission Expires May 19, 1936.

[fol. 687] [Title omitted]

AFFIDAVIT OF MALCOLM F. ORTON

CITY OF WASHINGTON,
District of Columbia, ss:

Malcolm F. Orton, being duly sworn on oath deposes and says:

I reside at Loudonville, New York, and I am Director of Research and Valuation of the Public Service Commission of the State of New York, having my office at the State Office Building, Albany, N. Y.

I graduated from Cornell University with degree of A. B. with honors in economics in 1920. In the last year, I was Reading Assistant in the Accounting Department. The work involved grading papers and examinations and general assistance in the work of the Department.

Prior to graduation, I was employed by Delos F. Wilcox, Consulting Public Utility Expert, at various periods commencing in 1909, amounting to 15 months in 1914-1915, 4 months in 1916, 9 months in 1919 and short intervals at [fol. 688] numerous other times. The work was a combination of private secretary and accountant and gave a general familiarity with problems of public utility regulation.

From November 1920 to November 1923 was employed by Marvyn Scudder & Company, Public Accountants. During this term my actual work was chiefly on public utility cases under the direction of Milo R. Maltbie. In 1923 I was employed directly by Mr. Maltbie and continued so with the exception of two months until March 1929.

During the entire period from 1920 to 1929 I was in charge of the accounting and statistical work on the following cases, among others:

Rate case involving rates of the New York Telephone Company in New York City and elsewhere in New York state. This included cases 7720, 377 and 1789 before the Public Service Commission and the case before the Special Master appointed by the Federal Court. I testified before the Special Master. The work included, in addition to ordinary accounting matters, the analysis of testimony by the company on valuation and annual and accrued depreciation and the preparation of basic data to be used in determining depreciation.

Jamestown Telephone Company rate and capitalization case in 1921-1922.

Rochester Telephone Company rate and capitalization case in 1921-1922.

Case involving New England Telephone and Telegraph Company before the New Hampshire Commission in 1925.

Case involving Bell Telephone Company of Canada be- [fol. 689] fore the Canadian Board of Railroad Commissioners in 1926.

Investigation into operations, cost and present value of Chicago surface lines and elevated roads made for the City of Chicago in 1924.

International Railway rate case in 1922.

Investigation into property and earnings of gas business of Central Kentucky Gas Company in City of Lexington in 1926.

Rate case involving New York Edison Company before Public Service Commission.

Rate case involving Iroquois Gas Company before New York Commission.

The work done on these cases varied in amount and responsibility but in general I had charge of the accounting work, examining the books and records to determine expenses and revenues, actual cost of the property and data to be used in making valuations and determining depreciation. During this period I also assisted in representing the City of New York before the Interstate Commerce Commission in Cases Nos. 14700 and 15100, involving the depreciation charges of telephone and steam railroad companies.

From October 1929 to April 1930 I was employed by Arthur Anderson & Company as a Senior Accountant, working on the audits of large utility companies.

From July 7, 1930 to the present date I have been employed by the Public Service Commission of New York as Director of Research and Valuation. In this position I have responsible supervision of the study of rates and rate structure of electric, gas and steam utilities under the Com- [fol. 690] mission's jurisdiction; allocations of cost between different classes of consumers; the preparation of uniform systems of accounts for various utilities, including telephone companies; examination of books and records of electric, gas and telephone utilities in connection with rate cases; the inventory and appraisal of property of electric, gas and telephone utilities; and other matters.

I have read the complaints filed by the American Telephone and Telegraph Company and Associated Companies, and by the Ohio Associated Telephone Company and Associated Companies, and the affidavits attached thereto. I am thoroughly familiar with the Uniform System of Accounts for Telephone Companies prescribed by the Federal Communications Commission, effective January 1, 1936, as well as with the various uniform systems of accounts previously prescribed for telephone companies by the Interstate Commerce Commission and by the New York Public Service Commission.

The various exceptions raised to the Uniform System of Accounts prescribed by the Federal Communications Commission, effective January 1, 1936, in the Bills of Complaint

and the opinions expressed in regard thereto in the affidavits are discussed below and my opinion thereon is stated.

1. Original Cost

A. The prescribed system of accounts shows the company's investment in telephone property upon the balance sheet in four items (considering for the moment only the asset side and ignoring the accounts for depreciation and amortization and for contributions). These four items are so numbered and designated as to obviously relate to property used or to be used in telephone service. The first three accounts are required to be stated at "original cost." The definition of "original cost", quoted in full in the Bills [fol. 691] of Complaint and each affidavit, is in effect the cost at the time of original construction. The fourth account shows the amount paid by the accounting company for the property, if any, in excess of the original cost. The total of the four accounts accordingly shows the actual cost of the property to the accounting company unless and until all or a portion of the amount carried in account 104, Telephone Plant Acquisition Adjustment, is written out of such account. Assuming for the moment that this has not been done except in regard to property actually retired from service, the accounts as prescribed will show in their total the exact figures which it is contended by the complainants and the affidavits supporting the complaint should be shown upon the balance sheet. In addition they show certain further information, namely, what the cost of the property was at the time of original construction and the subdivision of such cost between telephone plant in service, telephone plant under construction, and property held for future telephone use.

B. It therefore appears, ignoring for the moment the provisions regarding writing off of account 100.4, Telephone Plant Acquisition Adjustment, that the prescribed System of Accounts differs from that contended for by complainants only in that the amounts composing the actual cost of the property to the accounting company are subdivided instead of being shown as one lump sum. It is my opinion and appears to me to be obvious that such subdivision can not conceal any fact which would be relevant or interesting to the officers and directors of the corporation, to regulatory

commissions, to tax and other governmental authorities or to investors in the company's securities, as is charged [fol. 692] in the complaints and affidavits appended thereto. On the other hand, it is my opinion, based upon my experience in the regulation of public utilities, that the information afforded to Federal and state regulatory commissions by the subdivisions required to be made will be of great benefit in furthering the prompt and economical control of rates and capitalization. Furthermore, it is my opinion that such subdivision will be of great benefit to investors in the company's securities and to tax and other governmental authorities.

C. If the information proposed to be shown by these four subdivisions of the property accounts had been available to investors in securities of various public utilities, particularly telephone, electric, gas, and water utilities, it is my opinion that the inflation in the prices of these securities which occurred in the period 1920 to 1929, based in many cases upon the publication of balance sheets showing investments in operating property far in excess of the original cost of such investments, would have been materially less than actually occurred, with resulting material decrease in the losses sustained by investors in the period since 1929.

D. The affidavits of Messrs. Heiss and Young state at length that it is impracticable and expensive to determine the original cost of the present property. The amount of estimated expense depends of course upon what is required. It is my opinion, based upon experience in a position of responsibility for such determination, both by accounting and engineering methods, that such determination can be made with sufficient accuracy to be of value for the purposes above-mentioned without incurring excessive expense; that the estimate embodied in the affidavit of Mr. Young, [fol. 693] while it may be reasonable upon the plan of procedure upon which it is based, assumes determinations which are unnecessary; and that the actual expense necessarily incurred under the requirements of the Federal Communications Commission, will be materially less.

E. The Bills of Complaint and affidavits submitted therewith object to the provision of paragraph C of account 100.4 Telephone Plant Acquisition Adjustment, providing that

"the amounts recorded in this account with respect to each property acquisition shall be disposed of, written off, or provision shall be made for the amortization thereof in such manner as this commission may direct." This provision is interpreted as meaning that the commission may arbitrarily, without hearing or justification as a matter of correct accounting, at any time require the writing off of any portion or all of the balances contained in this account. I do not so interpret it. I do interpret it as meaning that the Commission will decide in the case of each acquisition, or perhaps in the case of the initial entry affecting all of the present property of the company in the case of the amounts then entered as a whole, what the accounting procedure shall be; and that this decision will be made after hearing, if hearing is desired by the company concerned, and will be based upon the general policy regarding accounting and the treatment of depreciation laid down by the Federal Communications Commission and its predecessor the Interstate Commerce Commission after extensive hearings, and upon sound accounting practice.

F. The necessity for leaving the prescription of detailed procedure upon these points until the cases actually arise lies in the fact that the entries to this account may represent [fol. 694] one or more of a large number of different factors. For example, they may represent the increase in value of the property acquired as compared with its original cost less depreciation on account of changes in general price levels or on account of particular local factors; they may represent high earning capacity of a property due to particularly favorable local conditions, to good management or to favorable treatment by local regulatory authorities; they may represent "nuisance value", the saving expected to be realized by the elimination of competition; or they may represent pure error in judgment on the part of the purchasing company. Particular attention should be called to the fact that in many cases of transfer of utility property constituting going plant from one corporate entity to another there is in fact no actual purchase and sale in the open market but the property is merely transferred from one corporation to another both of which are entirely controlled by a third which can fix the price at which the transfer shall be made at any amount which suits it, there being no difference in the ultimate effect whether the price is one dollar

or several million dollars since it is merely paid from one pocket into another so far as the parties interested are concerned.

G. It further appears that, far from representing an axe which may fall at any moment, the determination in this regard would normally be made as soon as all of the facts in regard to the transfer of property were available for consideration, and that once having been made in regard to a particular transfer it would not be subject to alteration or change. Furthermore, it is not to be assumed that amounts in this account which are properly chargeable to operating expenses will not so be charged. Specific provision is made for amortization and there is nothing in the [fols. 695 & 696] system of accounts which would prevent this being made to an operating expense account if the facts so justify.

H. Considerable stress is laid in the Bills of Complaint and in certain of the affidavits attached thereto upon the fact that the proposed accounting is "retroactive" in its effect upon telephone plants. The revised system requires a reclassification of existing plant. The complaints do not mention that the new system of accounts is in the same way "retroactive" in regard to all other balance sheet items, both assets and liabilities; neither do they state that the system of accounts prescribed by the Interstate Commerce Commission effective January 1, 1933, which they have been following and which they desire to be allowed to continue to follow, was in the same manner "retroactive" as regards all balance sheet items, including telephone plant; nor do they state that every system of accounts prescribed by any regulatory body in this country or, so far as I know, by any other governmental authority, has been "retroactive" in this sense, with one or two minor exceptions in regard to particular matters.

* * * * * * *

[fol. 697] 3. Distinction Between Accounts 100.1, 100.3 and 103

The Bills of Complaint allege that the accounting system is unreasonable in that the distinction as to whether property is to be accounted for in account 100.1, Telephone Plant

in Service, account 100.3, Property held for Future Telephone Use, and account 103, Miscellaneous Physical Property, is ambiguous and vague. This is a matter that can easily be determined by interpretations made from time to time as they appear necessary.

4. Treatment of Spare Plant

A. It is alleged in the Bills of Complaint and stated in the supporting affidavits that the prescribed accounting system is unreasonable and would cause excessive expenses in that it requires a separation to be made with great refinement between telephone plant in service and property held for future telephone use. Examples are given of the necessity for splitting the cost of a cable between these two accounts because certain pairs in such cable are used and certain other pairs are not used. I find nothing in the prescribed system of accounts which states or even implies that property which is used in telephone service, although not used to its full capacity, is to be split between two accounts. If there is any reasonable doubt as to whether or not the system requires this, an interpretation could have been and may now be obtained which will clear up such doubt. It is not to be assumed that an unreasonable degree of refinement is prescribed unless that is specifically and [fol. 698] clearly stated, either in a system of accounts or in the interpretation thereof.

B. Considerable space is given in the affidavit of Ben. F. Young to the immense expense, amounting in total to over $4,000,000, to the New York Telephone Company of segregating between the property to be entered in account 100.1, Telephone Plant in Service, and in account 100.3, Property Held for Future Telephone Use. It is my opinion that the expense as estimated by Mr. Young is based upon an incorrect interpretation of the requirements of the accounting system, and upon an extreme application of such interpretation. As a matter of practice it is expected that the property to be carried in account 100.3 would consist chiefly of parcels of land, either vacant or with buildings thereon. This would require no allocation whatsoever, but merely a determination as to an entire unit as to which account it should be carried in. In unusual periods of great fluctuations in business, there might be items of central office

equipment, or possibly entire banks of conduit, which would properly be carried in account 100.3. The determination of the amount of money involved in such cases would be relatively simple.

* * * * * * *

[fol. 699] 6. Requirement That Cost Shall Be Just and Reasonable

A. Objection is raised in the Bills of Complaint and supported in the affidavits attached thereto, to the provision that only just and reasonable costs shall be entered in the accounts for telephone plant and operating expenses and that any expenditures for such purposes which are not just and reasonable shall be entered elsewhere. The chief objection is that the provision is vague and indefinite and capable of various interpretations by different accounting officers. No proposal is made, or was made in the hearings and conferences before the Commission, as to any alternative proposal which would be more definite, but which would accomplish the same purpose of eliminating unjust and unreasonable expenses. Mr. Heiss goes further and argues that the accounts should reflect the actual expenditures even though unjust and unreasonable. This provision is particularly important in view of the control by holding company systems of all but a small fraction of the country's telephone business so that amounts paid for telephone plant and for purchases chargeable to operating expense are in a large part paid to affiliated companies and are not results of arms-length transactions. If any amounts paid, even though entirely unreasonable when measured by the property or services received in return therefor, are to be proper entries upon the books of the paying company, the officers and directors of such companies are relieved from all responsibility for the reasonableness of their expenditures. The burden thrown upon a regulatory commission [fol. 700] of determining whether the entries do actually represent the just and reasonable costs would be such as to destroy all effective regulation, since each and every entry, particularly those involving payments to affiliated companies, would have to be audited by the regulatory commission before any credence whatsoever could be attached to it, and audited not merely as to whether payment was

actually made, but as to whether property and services received were reasonable for the amounts paid.

B. Emphasis is laid by Mr. Heiss upon the burden thrown upon the accounting officer, and he appears to consider that the order prescribing the system of accounts applies to the accounting officer alone. This is not so. The order is served upon the company as a whole and applies to all officers and directors, and the responsibility for entering in the accounts only just and reasonable expenditures is upon all such officers and directors. The accounting officer is not required to decide as to the reasonableness of expenditures authorized by his superiors but can place the responsibility for such decision squarely upon them.

7. Impairment of Credit

A. It is alleged in the Bills of Complaint and supported in certain of the affidavits that the requirements of the new accounting system, particularly those as to the accounts to be shown upon the balance sheets and the basis of entries thereto, if put into effect and followed in the published balance sheets of the companies concerned, would seriously impair their credit. This allegation appears to be based primarily upon the provision for the segregation of the excess [fol. 701] of the cost to the accounting company over the original cost of the property acquired by purchase, less depreciation and amortization thereon, together with the provision that such excess may be required to be written off or amortized. In this connection the argument is made throughout that there is no difference between the entry of such excess in a separate account upon the asset side of the balance sheet in the group of accounts for telephone plant on the one hand, — the requirement that it be immediately written off to surplus on the other hand. This point has already been discussed from another angle under point 1 above. It is my opinion that the segregation of the excess cost upon the balance sheet will, in general, strengthen rather than impair the credit of the telephone companies. The facts in regard to such matters are already known to investment bankers and others interested in investment of funds on a large scale so that it is only the small investor who will be informed as to facts concerning which he was previously in ignorance. I conceive that it is desirable to

give such information and that it is the function of the regulatory commission to prescribe a system of accounts which will give it irrespective of possible adverse effect upon a small number of telephone companies. Certainly no investor will be misled by being given this information.

B. The Bills of Complaint contend further, however, that if the Commission requires that such excess cost be written off, investors will be misled by seeing the assets stated at an amount smaller than they really are, and thus be led to underestimate the net worth of the business. If this is so in the case of a company which has purchased a large amount of property from predecessor utilities, it must be so in the case of a company whose property was constructed at the same time but which has not been trans- [fol. 702] ferred from one owner to another by purchase. The complainants did not and do not propose to adjust the property accounts in the later case. It is my opinion that investors are more likely to interpret the facts clearly if a single uniform rule for the statement of telephone plant is followed which gives the same results irrespective of the history of the property as to whether or not it has remained under a single ownership or been transferred from one ownership to another. As a matter of fact, moreover, there is nothing in the system of accounts which would prevent the accounting company from informing the public as to the actual cost to it of its property irrespective of the treatment of the excess cost upon the books of account.

C. It is alleged in the affidavit of Andrew Sangster (page 9), that "were a prominent practicing accountant called upon to certify such balance sheet containing relatively substantial amount of said account, it would be his duty, in the opinion of this affiant, under the circumstances surrounding the status of that account, to require that a reserve of an equivalent amount be created out of the surplus, or authorized as a protection against possible extinction of the asset." If Mr. Sangster is correct, does it not follow that it would be equally the duty of a practicing accountant certifying to a balance sheet which contained the same total figure, but included in a single account, to require that the excess above the original cost be written off or covered by an adequate reserve? The actual assets and liabilities of the company concerned are the same in either case. The

only difference is that in the case which he cites the excess above the original cost is segregated in a separate account, and the regulatory commission, although specifically [fol. 703] reserving the right to order that it be written off or amortized, has not done so. In my opinion it follows that except in the unusual cases where the acquisition is recent and the matter of disposition of such excess is currently before the Commission for decision, the status of the amount as an asset is much better than under the alternative system advocated by the complainants.

8. Are Provisions Objected to Non-Severable from Remainder of the System

It is alleged in the Bills of Complaint and contended in all of the affidavits that the provisions objected to are non-severable and that they are inter-dependent with the other provisions of the system of accounts, and that if they are eliminated there is left an incomplete system under which it would be impracticable to keep proper books of account. This contention is sound only upon the legal theory that if the provisions of any account with reference to certain classes of property or transactions are found invalid, they are eliminated and nothing is or can be put in their place regarding such property or transaction, thus leaving an absolute blank in the system of accounts in these respects. Obviously if such is the case the system is incomplete and impossible of application if any account is eliminated. As a practical accounting matter, however, it is not, in my opinion, at all necessary that this should be the case. The complainant's objections are limited to a few specific accounts, and it would be entirely feasible, even if such objections were sustained, either temporarily, pending further investigation, or permanently to substitute in regard to such accounts the accounting procedure contended for by the complainants, but leave in full effect the prescribed system of accounts in regard to all other matters. Whether this can [fol. 704] be done as a matter of law, I do not profess to express an opinion, but as a matter of practical accounting I see no difficulty whatsoever.

* * * * * * *

[fol. 705] 10. Difference in Definition of Original Cost

A. Mr. Andrew Sangster alleges that the definition of original cost contained in the prescribed system is directly contrary to the definition of this same term as embodied in the uniform system of accounts for telephone companies, as prescribed by the Interstate Commerce Commission and in the uniform system of accounts for gas and electric companies, adopted by the National Association of Railway and Utilities Commissioners in November 1922. He states "original cost in all those systems of accounts means actual money cost to the accounting company." He implies, but does not state, that this definition is applied in those systems in cases where property is purchased as going plant rather than constructed by the accounting company. There is of course no difference between the original cost and cost to the accounting company in the case of property constructed by it, so that his criticism has no reason for being stated at all unless he intends to imply that original [fol. 706] cost has been used in these systems as meaning the purchase price paid for property acquired as going plant.

B. In the case of the Interstate Commerce Commission, Mr. Sangster's conclusion is directly contradicted by that Commission itself. In its report in Case No. 25705, dated July 9, 1934 (Exhibit A attached to complaint), it said:

"This (recommendation of the state commissions) would insert in instruction 3, Definitions, following paragraph (S) a definition of original cost. It is in substantial accord with the definition heretofore accepted by us. Montour R. Co. 33 Val. Rep. 681, 682. The continuity would be improved by a slight modification of the parenthetical phrase and a transposition of the word of. The last clause, while essentially surplusage, may emphasize and clarify the intent.

The proposed definition should be adopted, with the modifications indicated, as follows:

(S.1) Original cost means the actual money cost of (or the current money value of any consideration other than money exchanged for) property at the time when it was first devoted to the public service, whether by the accounting company or by a predecessor public utility."

[fol. 707] C. Examination of the Uniform Classification of Accounts for Electric Utilities adopted by the National Association of Railroad and Utility Commissioners in 1922 indicates that the term "original cost" appears two or three times and is used only in connection with the determination of the credits for property retired. In this connection it is used as synonymous with "the amount at which such thing stood charged in the capital account." It is nowhere used in connection with the amount to be charged to the capital account for property constructed or purchased and therefore is not used in the opposite sense to that in which it is defined in the prescribed system under consideration. The same is true of the Uniform Classification of Accounts for Gas Utilities.

Malcolm F. Orton.

Subscribed and sworn to before me this 10th day of December, 1935. Rosel H. Hyde, Notary Public. My commission expires May 19, 1936.

[fol. 708] [Title omitted]

AFFIDAVIT OF CHARLES W. SMITH

DISTRICT OF COLUMBIA,
City of Washington, ss:

Charles W. Smith, being duly sworn, on oath deposes and says:

1. I reside at Baltimore, Maryland.

2. (A) I have a B. S. degree in Finance and Business Administration and an LL.B. degree; I am a certified Public Accountant of North Carolina and of Maryland, and a member of the Maryland Bar. I am a past president of the Maryland Association of Certified Public Accountants and at present the Chairman of its Committee on Technical Subjects; I am also a member of the American Association of University Instructors in Accounting.

(B) From 1920 to 1929, I was employed as an auditor by the Income Tax Unit of the United States Treasury Department. As a result of obtaining the highest mark in a

competitive examination, I was appointed Chief Auditor of the Public Service Commission of Maryland on June 1, 1929, which position I still hold. As Chief Auditor of the Public Service Commission of Maryland, I have performed the usual duties of that office, such as, the making of audits and examinations of public utilities (including the Chesapeake and Potomac Telephone Company of Baltimore [fol. 709] City), making reports of such examinations and investigations, and testifying in regard thereto as well as in regard to statistical, financial, and economic matters.

(C) I have taught accounting in the leading schools of accounting in Baltimore City, and since 1930 I have been an instructor at Johns Hopkins University, where I teach Cost Accounting and Specialized Accounting, the latter sometimes being called Accounting Systems. I have made many addresses on accounting subjects and have discussed that subject over the radio on two occasions. I have acted many times as a consulting accountant.

3. I have examined and I am familiar with the Uniform System of Accounts for Telephone Companies, Issue of June 19, 1935, Effective January 1, 1936, prescribed by the Federal Communications Commission. I have read the bill of complaint, in Equity No. 81-366, of the American Telephone and Telegraph Company, et al., filed in the District Court of the United States for the Southern District of New York, and have also read the affidavits filed on behalf of the plaintiffs by Andrew Sangster, John T. Madden, Roy B. Kester, B. F. Young, and Charles A. Heiss. I have also read the bill of complaint of the Ohio Associated Telephone Company, Indiana Associated Telephone Corporation, Michigan Associated Telephone Company, Interstate Telephone Company, Pennsylvania Telephone Corporation, and Tri-State Associated Telephone Corporation, filed in the same proceedings.

4. (A) It is a fundamental and well-established principle of accounting that accounting systems must be so devised as to (a) conform to the recognized principles of accounting and (b) give the information desired in each particular case An accounting system which merely conforms to the recognized principles of accounting is not a proper accounting system. Before an accounting system can be devised or installed, it is necessary to have full information

[fol. 710] as to the purposes of the system, as to the nature of the reports to be made from that system, and as to the kind and extent of information required. The planning or devising of an accounting system which conforms to the recognized principles of accounting presents no difficulties; the planning or devising of an accounting system to give the needed information is a task that may well tax the ability of the most thoroughly trained accountant.

(B) It has long been recognized that if regulation of public utilities is to achieve any measure of success, uniform systems of accounts, which are sound in principle and which are well devised for the purpose of disclosing important facts, are essential. One of the first functions of regulatory commissions is the promulgation of accounting systems, and this has been true throughout the history of regulation in the United States. The information needed by a regulatory agency or by courts when they are called upon to decide questions involving the regulation of public utilities may differ substantially from information which is usually required for management purposes. The uniform system of accounts for public utilities which are now in existence have been designed, in the large, to supply essential information required by regulatory agencies, and to the extent that the accounting systems have been devised for the purpose of giving regulatory agencies proper information, there has occurred a departure in form, but not in substance, in the planning of accounting systems. It is, therefore, not only possible but also requisite that the accounting system conform to the sound principles of accounting but at the same time be so devised as to supply the information that is needed in each particular instance.

(C) It is my firm conviction that the accounting system promulgated by the Federal Communications Commission on June 19, 1935, is sound in principle. It is also my firm [fol. 711] conviction that said system will make available to the regulatory commissions, and to courts, much information needed in the regulation of telephone utilities. I give below my reasons for believing that the Uniform System of Accounts hereinbefore referred to is sound in principle, as well as my reasons for believing that the System is designed to give valuable information to regulatory agencies. My views will be confined to the questions or issues raised by the plaintiffs.

5. Plant Accounts

(A) The accounts of the Uniform System of Accounts are designed to show (a) the original cost of telephone plant in service, (b) the original cost of plant held for future use, and (c) the cost to the company of telephone plant. The original cost of plant or fixed capital in service should be presented in every valuation case. It is important information not only from the viewpoint of original cost per se but also because it is an admirable check on the other evidences of value which are usually introduced in valuation proceedings. If I were asked the value of any property, I would first ask the original cost of that property, together with the year which the cost was incurred. I might not know whether a certain building would have a fair value of one million dollars or five million dollars, but if I knew the original cost of that building, if I knew the date the cost was incurred, I should be able to pass intelligently upon other evidences of value which might be presented to me. The Supreme Court of the United States has very logically and very consistently held that original cost is one of the evidences of value, and public utility accountants throughout the country have been instructed to determine original cost wherever such determination is possible. Original cost cannot mean cost to the utility because such cost may bear no relationship whatever to the value of the physical properties at any time, whereas origi- [fol. 712] nal cost in its proper meaning is of great significance in determining the value at the time the costs were incurred. Original cost has had and still has a definite meaning in public utility accounting—and that meaning is the cost of the property at the time it was originally constructed (for practical purposes, cost to the person first devoting the property to public service is considered original cost). It is the practice of public utility accountants and engineers, both representatives of utilities and representatives of governments, to present data as to original cost to regulatory commissions, such data conforming to the definition of the term as used by me immediately above.

(B) The only means of ascertaining satisfactorily original cost, and without the expenditure of huge sums, is by prescribing an accounting system which will segregate the cost of fixed capital between the original cost and the cost to the utility. The Uniform System of Accounts prescribed

by the Federal Communications Commission accomplishes this purpose. The System was devised so as to conform to the sound principles of accounting, at the same time give valuable, essential information to regulatory bodies. The Accounting System does not provide that the plant accounts shall show original cost only. The System is devised to show the cost to the utility, the cost to the utility, however, being segregated between original cost and second, third, or fourth, etc., cost. If uniformity of accounting is to be achieved, it is necessary that the units of property which go to make up total telephone plant be valued on the same basis. If some of the units are stated at original cost, others at cost to the first vendee, others at cost to the second vendee, etc., a conglomeration results and hybrid figures are obtained, which will destroy uniformity and greatly lessen the value of any information derived from the system [fol. 713] of accounts. The Accounting System mentioned hereinbefore does not prevent the telephone utility from showing the total cost of its property in its record; it merely requires a segregation of cost for the purpose of obtaining information which courts and commissions, since regulation first began, have held is necessary.

(C) Telephone Plant Acquisition Adjustment.—Account 100.4, Telephone Plant Acquisition Adjustment, together with certain other accounts, such as reserves, measures the difference between the original cost of plant and the cost to the accounting utility. The text of that account provides how the amounts therein shall be disposed of.

"The amounts recorded in this account with respect to each property acquisition shall be disposed of, written off, or provision shall be made for the amortization thereof in such manner as this Commission may direct."

The requirement is reasonable. Much information is needed as to the nature of the amounts recorded in this account before intelligent provision for disposing of such accounts can be made. The amounts may represent intangibles. They may result from transactions between affiliated companies or transactions which are not at arm's length. They may represent nuisance values or many other conceivable values. Before a final disposition of Account 100.4 can be made, it therefore becomes necessary to have an analysis of the ac-

count. It is my belief that when the Federal Communications Commission and other regulatory commissions are in full possession of the facts, they will act reasonably, fairly, and legally in ordering the disposition of the amounts recorded in said Account 100.4. No question of accounting principle is here and now presented; the only question which can arise is as to the nature of the Commission's action when the Commission does act. It is an unwarranted presumption to say that the Commission will arbitrarily or capriciously order the charging off of amounts in Account 100.4. It is not likely [fol. 714] that the amounts, if any, and the nature thereof, includible in Account 100.4, will be known prior to December 31, 1936, so that it is premature to judge how the disposition of such accounts, if any, will be ordered. No accounting principle, however, can possibly be involved in this matter until an order covering the disposition of any amounts in that Account has been promulgated. Affiant, therefore, firmly believes that Account 100.4 is sound in principle and will be sound in practice, and that said Account will give valuable information to everyone concerned with the regulation of telephone companies.

(D) Property Held for Future Telephone Use.—The purpose of this account is to show the original cost of property owned and held in telephone service under a definite plan for telephone usage. Property which is not in service and which is not producing revenue should be segregated from property which is used productively. No principle of accounting is violated by separating the property which is not in use from property which is in use. It is true that the capricious and arbitrary interpretation of the Account might well become a burden to the utility, but a just, fair, and reasonable interpretation of the Account would serve to give information which is needed in every valuation proceeding. I believe that it is not contemplated that parts of property shall be segregated so that certain parts thereof will be included in plant in service and other parts included in property held for future use. It is my firm belief that, when the question is properly presented to any regulatory agency which has authority to act as to whether unused wires in cable shall be classified as plant in service or plant held for future use, the interpretation will be that the original cost of such wires shall be included in Account 100.1, Telephone Plant in Service. This matter, again, does

not involve any accounting principle: it merely involves an interpretation which has not as yet been given. An ad- [fol. 715] mirable illustration of the use of the Account is where land is purchased as a prospective site for an office building under a definite plan: that land, prior to the time of construction, should be excluded from Account 100.1, Telephone Plant in Service, because the land is not in service, but should be in account 100.3, Property Held for Future Telephone Use. I reiterate that the account is sound, and I believe its interpretation will be reasonable.

* * * * * * *

[fol. 716] 7. Depreciation.—There is no subject in the entire realm of accounting concerning which there is greater controversy. There are certain definite and well recognized principles of depreciation accounting, but when it comes to public utility accounting, there is a great deal of conflict as to the method which should be employed in computing depreciation expense. The depreciation principles recognized by the Uniform System of Accounts for Telephone Companies, hereinbefore referred to, are sound, are conservative, and conform to the best practice of accountants. The reading of the bills of complaint indicates that the plaintiffs raise only two issues in regard to depreciation accounting as required by the Uniform System, and these are (a) that no provision is made for depreciating Account 100.3, Property Held for Future Telephone Use, and (b) that no provision is made for depreciating Account 100.4, Telephone Plant Acquisition Adjustment.

* * * * * * *

[fol. 717] (B) I have stated hereinbefore my views in regard to amortizing or depreciating or writing off the amounts, if any, which will ultimately rest in 100.4, Telephone Plant Acquisition Adjustment. I reiterate that until all the facts in regard to the amounts in that Account become available, it is premature to judge any action of the Commission. The Uniform System of Accounts violates no principle of accounting in regard to Account 100.4, and no principle of accounting can be violated until the amounts included therein have been ascertained and further accounting instructions or orders in regard thereto promulgated or issued.

8. Just and Reasonable Charges

The bill of complaint and the affidavits on behalf of the plaintiffs attack the provision of 2 B. 1 (page 2) of the Uniform System of Accounts, which provision reads as follows:

[fol. 718] "All charges to the accounts prescribed in this classification for telephone plant, income, operating revenues, and operating expenses shall be just and reasonable and any payments by the company in excess of such just and reasonable charges shall be included in account 323, 'Miscellaneous income charges.'"

It is again my firm conviction that unjust and unreasonable charges must be segregated from just and reasonable charges. If unjust and unreasonable charges are to be included in the telephone plant income, operating revenue, or operating expense accounts, then the Accounting System will have failed of its purpose, which is to give sound accounting information to regulatory agencies. The principle involved herein, like many principles of accountancy, must be interpreted and practiced in accordance with the rule of reason. It may be difficult in rare instances to determine whether a charge is just or reasonable, but on the other hand, in most instances no such difficulty will be encountered. In my opinion, the provision is not only reasonable but is absolutely necessary. It should not be forgotten that public utilities are usually monopolies, and it should be remembered that transactions between public utilities are not always at arm's length, so that it is vital for regulatory commissions and others concerned with regulatory problems to be fully informed if they are to act intelligently. If unjust and unreasonable charges are permitted to find their way into the accounts, it must be recognized that the entire accounting system will fail of its intended effect. In this connection, it should be recalled that the Revenue Act of 1934 (Section 23(m)) and preceding revenue acts permit as deductions for income tax purposes "ordinary and necessary" expenses. An expense may be just and reasonable and still unnecessary. The added burden of determining those unnecessary expenses which are also unjust and unreasonable would appear to be slight.

9. In conclusion, I again affirm that it is my firm convic-[fol. 719] tion that the Uniform System of Accounts issued June 19, 1935, and effective January 1, 1936, promulgated by the Federal Communications Commission, is sound in principle in that it violates no recognized principle of accounting, and that it is well designed to give interested governmental agencies, including courts, investors, and others, necessary and vital information which cannot be obtained in any other manner.

Chas. W. Smith.

Subscribed and sworn to before me this 11th day of December, 1935. M. Aileen Botton, Notary Public. My commission expires June 10, 1938.

[fol. 720] Objection of United States of America

To the submission and reception of the aforesaid affidavits in support of and in opposition to said applications, defendant, United States of America, while not objecting to their use as a method of trying the case, objected "on the ground that they contain matters dealing with the legal effect of the system of accounts and constitute a usurpation of the function of the court and are not proper evidentiary matter to prove the issues in this case and are inadmissible for the reasons stated in Mississippi Valley Barge Line case, 292 U. S. 282." To the court's ruling and reception thereof as expert, proper and material evidence, said de*fendant noted an exception.*

Motions to Dismiss

A motion was made by defendant, United States of America, and joined in by defendant, Federal Communications Commission, to dismiss the aforesaid applications and the respective bills of complaint of plaintiffs and additional plaintiffs, and the bill of intervention of intervening plaintiffs.

Stipulation as to Submission

Thereupon, and at the conclusion of said hearing, it was orally stipulated and agreed by all parties in open court that the cause be submitted for final hearing and decree,

and not only for decision on the applications for a temporary restraining order and an interlocutory injunction, upon the pleadings and the affidavits aforesaid, subject to the aforesaid objection as to the materiality thereof, pro- [fol. 721] vided that plaintiffs might file rebuttal affidavits, subject to the aforesaid objection as to materiality. Whereupon the court reserved decision upon said applications for an interlocutory injunction and upon said motions to dismiss, and granted a stay pending final decision, which order was filed herein on the 28th day of December, 1935.

Within the time set by the court, plaintiffs filed the affidavit in rebuttal of Andrew Sangster; the affidavit in rebuttal of John T. Madden; the affidavit in rebuttal of Roy B. Kester; the affidavit in rebuttal of B. F. Young; and the affidavit in rebuttal of Charles A. Heiss, all verified on the 17th day of December, 1935, and filed herein on the 18th day of December, 1935. Said affidavits in rebuttal respectively are as follows:

[fol. 722] [Title omitted]

AFFIDAVIT OF ANDREW SANGSTER ON BEHALF OF PLAINTIFFS, IN REBUTTAL

STATE OF NEW YORK,
County of New York, ss:

Andrew Sangster, being duly sworn on oath, deposes and says:

I have read the affidavits of William J. Norfleet, Robert S. Rains, John H. Bickley, Asel R. Colbert, Malcolm F. Orton and Charles W. Smith verified on the 11th day of December, 1935, and filed herein. I find nothing therein [fol. 723] which causes me to withdraw or modify my original affidavit herein, verified by me on the 5th day of December, 1935, and I hereby reaffirm said original affidavit.

(Sgd.) Andrew Sangster.

Subscribed and sworn to before me, this 17th day of December, 1935. (Sgd.) Charles M. Deal, Notary Public. Notary Public, Kings Co., No. 363, Reg. No. 7148. Cert. Filed in N. Y. Co. No. 393, Reg. No. 7-D-225. Commission Expires March 30, 1937. (Seal Charles M. Deal, Notary Public.)

[fol. 724] [Title omitted]

AFFIDAVIT OF JOHN T. MADDEN ON BEHALF OF PLAINTIFFS, IN REBUTTAL

STATE OF NEW YORK,
County of New York, ss:

John T. Madden, being duly sworn on oath, deposes and says:

I have read the affidavits of William J. Norfleet and Robert S. Rains verified on the 11th day of December, 1935, and filed herein. I find nothing therein which causes me to withdraw or modify my original affidavit herein, verified by me on the 6th day of December, 1935, and I hereby reaffirm said original affidavit.

[fol. 725] I have been asked by the solicitors for the plaintiffs to read the affidavits of John H. Bickley, Asel R. Colbert, Malcolm F. Orton and Charles W. Smith, filed herein, but due to other engagements I have not had time to read any of them.

(Sgd.) Jno. T. Madden.

Subscribed and sworn to before me, this 17th day of December, 1935. (Sgd.) Charles M. Deal, Notary Public. Notary Public, Kings Co., No. 363, Reg. No. 7148. Cert. Filed in N. Y. Co. No. 393, Reg. No. 7-D-225. Commission Expires March 30, 1937. (Seal Charles M. Deal, Notary Public.)

[fol. 726] [Title omitted]

AFFIDAVIT OF ROY B. KESTER ON BEHALF OF PLAINTIFFS, IN REBUTTAL

STATE OF NEW YORK,
County of New York, ss:

Roy B. Kester, being duly sworn on oath, deposes and says:

I have read the affidavit of John H. Bickley verified on the 11th day of December, 1935, and filed herein. I find nothing therein which causes me to withdraw or modify my original affidavit herein, verified by me on the 6th day of

December, 1935, and I hereby reaffirm said original affidavit.

I have been asked by the solicitors for the plaintiffs to read the affidavits of William J. Norfleet, Robert S. Rains, [fols. 727–730] Asel R. Colbert, Malcolm F. Orton and Charles W. Smith, filed herein, but due to other engagements I have not had time to read any of them.

(Sgd.) Roy B. Kester.

Subscribed and sworn to before me, this 17th day of December, 1935. (Sgd.) Charles M. Deal, Notary Public. Notary Public, Kings Co., No. 363, Reg. No. 7148. Cert. Filed in N. Y. Co. No. 393, Reg. No. 7-D-225. Commission Expires March 30, 1937. (Seal Charles M. Deal, Notary Public.)

[fol. 731] [Title omitted]

AFFIDAVIT OF CHARLES A. HEISS ON BEHALF OF PLAINTIFFS, IN REBUTTAL

STATE OF NEW YORK,
County of New York, ss:

Charles A. Heiss, being duly sworn, on oath deposes and says:

I am the same Charles A. Heiss who made an affidavit herein dated December 6, 1935.

I

I have read the affidavit of William J. Norfleet dated December 11, 1935, filed by the defendants herein, at page 18 of which the following statement is made:

"3. It is my opinion and understanding that this Com- [fol. 732] mission's system of accounts permits the recording of necessary 'stand-by' plant in Account 100.1, 'Telephone plant in service' and that periodical transfers between said Account 100.1 and Account 100.3, 'Property held for future telephone use' will not be required by reason of seasonable changes or fluctuating demands for plaintiffs' services. It is also my understanding that such interpreta-

tion was discussed and made clear at the conference between representatives of this Commission and representatives of plaintiffs and other telephone companies relating to the then proposed system of accounts for telephone companies, on May 16, 1935."

I represented the plaintiffs at the conference referred to at which criticisms were made of the tentative draft of a system of Accounts which had been issued with Telephone Division Order No. 7-B of the Commission. At said conference, in reply to inquiries by representatives of the telephone companies, one of the Commission's accountants made a statement to the effect that Account 100.3, "Property Held for Future Telephone Use," was not intended to include all spare plant. No stenographic transcript of the conference or of the aforesaid statement of the Commission's accountant was made. Being of the opinion that said statement would not be considered as something to be read into the system of accounts, and desiring to have it made more definite and to have it adopted by the Commission, I wrote the Commission on May 24, 1935, asking that certain provisions of the tentative system of accounts (Instruction 3-BB, Account 100.1, "Telephone Plant in Service," and Account 100.3, "Property Held for Future Tele-
[fols. 733 & 734] phone Use") be changed so as to provide that Account 100.1 and the telephone plant accounts (the 200 series) should include "spare plant temporarily not in use" and that Account 100.3 should not include such spare plant. In the "Issue of June 19, 1935," which was subsequently prescribed by Telephone Division Order No. 7-C of that date, the Commission completely ignored this request, left the text of the tentative system with regard to Instruction 3-BB, Account 100.1 and Account 100.3 unchanged, and incorporated in the final system neither my requested change, the interpretation referred to by affiant Norfleet, above set forth, nor any other clarifying language.

My letter of May 24, 1935, to the Commission is the 78-page statement of exceptions referred to on page 4 of the answer of the defendant Federal Communications Commission herein. The Commission adopted some of the suggestions contained in said letter and embodied them in said "Issue of June 19, 1935," and I concluded that its failure to adopt the suggested changes specified above constituted a refusal to adopt the interpretation suggested by its ac-

countant and an insistence that the provisions above referred to stand as written.

[fol. 735] I have read the affidavits of William J. Norfleet, Robert S. Rains, John H. Bickley, Asel R. Colbert, Malcolm F. Orton and Charles W. Smith verified on the 11th day of December, 1935, and filed herein. I find nothing therein which causes me to withdraw or modify my original affidavit herein, verified by me on the 6th day of December, 1935, and I hereby reaffirm said original affidavit.

(Sgd.) Charles A. Heiss.

Subscribed and sworn to before me, this 17th day of December, 1935. (Sgd.) Charles M. Deal, Notary Public. Notary Public, Kings Co., No. 363, Reg. No. 7148. Cert. Filed in N. Y. Co. No. 393, Reg. No. 7-D-225. Commission Expires March 30, 1937. (Seal Charles M Deal, Notary Public.)

[fol. 736] The above and foregoing is all the evidence introduced by the respective parties on the final hearing on the merits and for a permanent injunction in this cause, as provided in the foregoing stipulation, and is essential for the decision of the questions presented by the appeal herein to the Supreme Court of the United States.

Wherefore plaintiffs-appellants, additional plaintiffs-appellants, and intervening plaintiffs-appellants, pray that the above Statement of Evidence be approved and allowed by the above entitled court as a true, complete and properly prepared statement of all the evidence taken and given on the final hearing of said cause, and essential for the decision of the questions presented by the appeal herein to the Supreme Court of the United States.

Dated May 12, 1936.

C. M. Bracelen, Chas. T. Russell, Edward L. Blackman, Alan J. McBean, Solicitors for Plaintiffs and Intervening Plaintiffs. Allen T. Klots, Halen N. Smith, Solicitors for Additional Plaintiffs.

[fol. 737] IN UNITED STATES DISTRICT COURT

[Title omitted]

STIPULATION AS TO STATEMENT OF EVIDENCE AND WAIVER OF LODGMENT AND NOTICE OF FILING—Filed May 13, 1936

It is hereby stipulated and agreed by and between the parties hereto, by their respective counsel, that the above and foregoing Statement of Evidence, having been examined and read by said respective counsel, is a true and correct statement under Paragraph b of Equity Rule 75, and that the copies of all affidavits and appendices thereto [fol. 738] attached, included in said statement are true and correct copies of the originals filed in this court in the above entitled cause, and that they shall be treated and accepted in all respects the same as the originals filed in this cause, and that the same may be incorporated in the transcript of the record by the clerk of this court on the appeal in this cause to the Supreme Court of the United States.

It is further stipulated and agreed that the lodgment of said Statement of Evidence in the clerk's office for the examination of defendant, United States of America, defendant, Federal Communications Commission, and intervening defendant, National Association of Railroad and Utilities Commissioners, and notice of such lodgment and of the time when same will be presented to the court for approval are hereby waived by said defendants and intervening defendant, and the same may be approved by the court at once, and when so approved may be filed in the clerk's office and become a part of the transcript of record in this cause on appeal to the Supreme Court of the United States.

Dated: May 12, 1936.

C. M. Bracelen, Chas. T. Russell, Edward L. Blackman, Alan J. McBean, Solicitors for Plaintiffs and [fol. 739] Intervening Plaintiffs. Allen T. Klots, Hayden N. Smith, Solicitors for Additional Plaintiffs. Harold F. Collins, Special Assistant to the Attorney General, Solicitor for Defendant, United States of America. Hampson Gary, Frank Roberson, W. D. Humphrey, Solicitors for Defendant, Federal Communications Commission. John E. Benton, Solicitor for Intervening Defendant, National Association of Railroad and Utilities Commissioners.

[fol. 740] In United States District Court

[Title omitted]

Order Approving Statement of Evidence—Filed May 13, 1936

On this 13th day of May, 1936, the foregoing Statement of Evidence having been presented to me, and the parties having stipulated and agreed thereto, the same is hereby in all things allowed and approved, and the same is hereby ordered filed as a Statement of Evidence to be included in the record on appeal to the Supreme Court of the United States in the above entitled cause, as provided in Paragraph b of Equity Rule 75.

Jno. C. Knox, United States District Judge.

Dated, New York, N. Y., this 13th day of May, 1936.

[fol. 741] In United States District Court

[Title omitted]

[fol. 742] Order Granting Temporary Stay—Filed December 28, 1935

This Cause came on to be heard before the Honorable Martin T. Manton and the Honorable A. N. Hand, Circuit Judges of this Circuit, and the Honorable John C. Knox, District Judge of this District on the 13th and 14th days of December, 1935 pursuant to the Order to Show Cause herein dated the 6th day of December, 1935, upon the application of the plaintiffs for an interlocutory injunction, suspending during the pendency of said cause the operation of that certain order of the Federal Communications Commission, designated "Telephone Division Order No. 7-C," dated June 19, 1935, effective January 1, 1936, prescribing a Uniform System of Accounts for Telephone Companies, and for a temporary stay of the operation of said order pending the determination of said application for an interlocutory injunction, and was argued by Counsel.

And the parties having stipulated in open court to submit the case for final decree upon the pleadings, affidavits [fol. 743] and briefs filed and to be filed, as directed by the Court at said hearing;

Now, therefore, pursuant to the provisions of the Urgent Deficiencies Appropriations Act (38 Stat. L. 219, 220, Code of Laws of the United States, Title 28, sections 41 (28), 43-48 inclusive, and particularly Section 47 of said Title), the Court finds:

1. That said plaintiffs, additional plaintiffs and intervening plaintiffs (hereinafter referred to as plaintiffs) are carriers subject to the Communications Act of 1934;

2. That said plaintiffs are telephone companies subject to the terms of said "Telephone Division Order No. 7-C" of the Federal Communications Commission;

3. That under the terms of said order said plaintiffs will be required to install on January 1, 1936 a system of accounts in accordance therewith which is materially different from that prescribed by the Interstate Commerce Commission, now in effect;

4. That if a temporary stay is not granted pending the decision herein irreparable damage will result to plaintiffs, [fol. 744] in that said "Telephone Division Order No. 7-C" by its terms will require them to install and put into operation on January 1, 1936, in lieu of the system of accounts now kept in conformity with law, a new system of accounts materially and essentially different therefrom, as prescribed by said "Telephone Division Order No. 7-C"; that said changed method of accounting will require an extensive restatement of the accounts of said plaintiffs and entail the expenditure of substantial sums of money over and above the cost of keeping the present prescribed system of accounts; all as shown by the affidavits of Charles A. Heiss and B. F. Young on the part of plaintiffs;

Wherefore it is now ordered, adjudged and decreed that the operation of said "Telephone Division Order No. 7-C" of the Federal Communications Commission be stayed and suspended until the final decision of this Court, or until [fol. 745] the further order of the Court.

Dated December 27th, 1935.

By the Court:

Martin T. Manton, Circuit Judge. Augustus H. Hand, Circuit Judge. Jno. C. Knox, District Judge.

[fol. 746] IN UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

AMERICAN TELEPHONE AND TELEGRAPH COMPANY et al., Plaintiffs,

against

UNITED STATES OF AMERICA AND FEDERAL COMMUNICATIONS COMMISSION, Defendants

Before Martin T. Manton and Augustus N. Hand, Circuit Judges, and John C. Knox, District Judge, Constituting a Statutory Court under 28 U. S. C. 47

C. M. Bracelen, Esq., Chas. T. Russell, Esq., Edward L. Blackman, Esq., Alan J. McBean, Esq., Solicitors for Plaintiffs, and Eastern Tel. & Tel. Co., et al. Allen T. Klots, Esq., Hayden N. Smith, Esq., Solicitors and Counsel for Ohio Associated Telephone Co. et al., Additional Plaintiffs. Winthrop, Stimson, Putnam & Roberts, G. Schuyler Tarbell, Jr., of Counsel.

Harold F. Collins, Esq., Special Assistant to the Attorney General. Albert E. Stephen, Esq., W. D. Humphrey, Esq., for Federal Communications Comm. Hampson Gary and Frank Roberson, of Counsel.

[fol. 747] Clyde S. Bailey, Esq., John E. Benton, Esq., Attorneys for National Assn. of Railroad & Utilities Commissioners.

Charles G. Blakeslee, Esq., Solicitor for Public Service Commission of the State of New York.

OPINION—Filed February 18, 1936

MANTON, Circuit Judge:

Plaintiffs, common carriers of communication by wire, file this bill under the Urgent Deficiencies Act, October 22, 1913, c. 32, 38 Stat. 208, 219, made applicable by § 402(a) of the Communications Act [June 19, 1934, c. 652, § 402(a), 47 U. S. C. 402(a), 48 Stat. 1093]. They seek to restrain the Federal Communications Commission from enforcing its Order No. 7-C issued June 19, 1935 and effective January 1, 1936 to govern the system of accounts for telephone companies engaged in interstate commerce and having average annual operating revenues exceeding $50,000. A tem-

porary stay was granted pending decision on the permanent injunction. The issues are submitted for final determination on affidavits and the arguments thereon.

The accounting system now in operation was promulgated by the Interstate Commerce Commission as the "Uniform System of Accounts for Telephone Companies, First Revised Issue," effective from January 1, 1933. Upon objections by twenty-two state commissions, the Interstate Commerce Commission had taken under advisement suggested changes in this 1933 system. Its inquiry ended very shortly before jurisdiction over telephone companies was transferred to the Federal Communications Commission created by the Communications Act of June 19, 1934. In view of this fact, the Interstate Commerce Commission, although it issued no order, rendered a report of the pro- [fol. 748] ceedings before it, for the convenience of the incoming Commission [Accounting Rules for Telephone Companies, 203 I. C. C. 13]. In this report, some of the matters now objected to, were discussed and disapproved. The Communications Commission, after supplemental investigation, hearings and conferences, did not follow the Interstate Commerce Commission in its disapproval of these provisions and incorporated them in the system now under review. The National Association of Railroad and Public Utility Commissioners, which claims to represent the commissions having jurisdiction over telephone companies in forty-six states, has endorsed the proposed system and has appeared in this case by intervening as a party defendant. In addition, the New York State Public Service Commission pleads for the order as amicus curiæ.

The attack on the order requiring the uniform system of accounts is based upon the claim that it is invalid because it violates the Fifth Amendment to the Constitution and § 404 of the Communications Act, (a) since it is unsupported by a report stating conclusions and basic findings; (b) the requirements exceed the statutory power of the Commission and are so contrary to the fundamental principles of correct accounting as to constitute an abuse of that power in so far as they treat of original cost, contributions, certain classifications of telephone plant and depreciation thereon, and just and reasonable charges; (c) amendments in requiring obedience to standards so vague and indefinite as to be unintelligible, or violate the Fifth and Sixth Amendments.

Before other discussion, it should be settled that the order is not void for lack of a report stating the conclusions and findings of fact by the Commission. Section [fol. 749] 220(a) of the Communications Act provides:

"The Commission may, in its discretion, prescribe the forms of any and all accounts, records, and memoranda to be kept by carriers subject to this chapter * * *."

There is an identical provision in the Interstate Commerce Act, § 20(5). When a system of accounts is laid down under these sections, the action is a legislative, rather than a judicial function. It is making a new rule to be applied in the future, not applying an already existent rule to past facts. This is the characteristic of legislation. See: Keller v. Potomac Electric Power Co., 261 U. S. 428, 440; Prentis v. Atlantic Coast Line Co., 211 U. S. 210, 226. And to claim that findings are essential to support this order is to ignore this difference. Assigned Car Cases, 274 U. S. 564, 583. An administrative body can exercise a delegated legislative function without first reporting the data upon which it decided that the proposed rule should be established. Pacific States Box & Basket Co. v. White, 80 L. Ed. 133. Since the Commission is authorized to act "in its discretion", there is no requirement that it find the facts upon which its authority to act is conditioned as in Atchinson, Topeka & Santa Fe Ry. Co. v. United States, 295 U. S. 193; United States v. Chicago, Milwaukee, St. Paul & Pac. R. Co., 294 U. S. 499; United States v. Baltimore & Ohio R. R. Co., 293 U. S. 454. The case last cited points out the difference at p. 462. In holding an order void for lack of a finding on a jurisdictional fact, the court said:

"The Act (Boiler Inspection Act) does not confer upon the Commission legislative authority to require the adop- [fol. 750] tion on locomotives of such services as, *in its discretion*, it may from time to time deem desirable."

Section 220(a) conferring power to prescribe the accounting system does confer upon the Commission power to act in its discretion.

Nor does § 404 of the Act render an order under § 220(a) void if a report is lacking. Section 404 provides:

"Whenever an investigation shall be made by the Commission it shall be its duty to make a report in writing

in respect thereto, which shall state the conclusions of the Commission, together with its decision, order or requirement in the premises; and in case damages are awarded such report shall include the findings of fact on which the award is made."

This section requires findings of fact only in the event damages are awarded. The order No. 7-C does not award damages. Although the Commission, as outlined above, did extensive preliminary work before entering the order, a report of its conclusions is not a condition to the order's validity. The conclusions of the Commission are very evident from the order itself.

In support of this position, there is the fact that § 404 and 220(a) of the Communications Act are identical with § 14(1) and § 20(5) of the Interstate Commerce Act. It has not been the practice of the Interstate Commerce Commission to preface its general accounting orders with reports, and the incorporation of these sections in the Communications Act is an indication that Congress approved this administrative interpretation. See: McGaughen v. Hershey Chocolate Co., 283 U. S. 488, 492, 3; National Lead [fol. 751] Co. v. United States, 252 U. S. 140, 146.

The Communications Act made the judicial procedure applicable in proceedings to enforce or test the validity of the Communications Commission orders similar to like proceedings affecting the orders of the Interstate Commerce Commission (§ 402[a]). We must, therefore, in reviewing this order, be guided by the rule that in respect to orders of the Commission, the court may not "under the guise of exerting judicial power, usurp merely administrative functions by setting aside a lawful administrative order upon our conception as to whether the administrative power has been wisely exercised." Interstate Commerce Comm. v. Illinois Central R. R. Co., 215 U. S. 452, 470. See: Interstate Commerce Comm. v. Union Pacific R. R. Co., 222 U. S. 541, 547. It is not enough to reason that the order is unwise, inexpedient or at variance with the court's own views as to what is practicable. This rule guides judicial review of any legislative act. Chicago, Burlington & Quincy R. R. Co. v. McGuire, 219 U. S. 549, 569.

We have already pointed out that the order prescribing a uniform system of accounts is of a legislative character. When § 20(5) of the Interstate Commerce Act was before

the Supreme Court in Interstate Commerce Commission v. Goodrich Transit Co. (224 U. S. 194) and Kansas City Southern Railway Co. v. United States (231 U. S. 423), the court, while characterizing the Commission's power as legislative, also held it not unlawfully delegated, saying, at 214:

"The Congress may not delegate its purely legislative power to a commission, but, having laid down the general rules of action under which a commission shall proceed, [fol. 752] it may require of that commission the application of such rules to particular situations and the investigation of acts, with a view to making orders in a particular matter within the rules laid down by the Congress * * *."

And referring to § 20, said:

"* * * The Commission is permitted, in its discretion, to require a uniform system of accounting, and to prohibit other methods of accounting than those which the Commission may prescribe. In other words, Congress had laid down general rules for the guidance of the Commission, leaving to it merely the carrying out of details in the exercise of the powers so conferred. This, we think, is not a delegation of legislative authority."

No commission accounting order is to be reviewed judicially for the purpose of determining whether it conforms to the court's views as to what constitutes proper, efficient, practical accounting methods but it is for the court to say only whether the commission has acted within statutory and constitutional limits. See, Norfolk & Western R. R. Co. v. United States, 287 U. S. 134, 143.

Therefore, our inquiry as far as it goes beyond a consideration of power within the statute is merely whether the order is "so entirely at odds with fundamental principles of correct accounting as to manifest an abuse of power." See, Chesapeake & Ohio Ry. Co. v. United States, 5 Fed. Supp. 7, 14 (E. D. N. Y.).

Section 213(c) in specific terms authorized the commission to obtain from telephone carriers at any time informa- [fol. 753] tion concerning original cost of their properties which may be needed for rate fixing purposes. And it is asserted by plaintiffs, that this section is the full measure of the Commission's authority to require information as

to original cost and that an order under § 220(a) requiring data in respect of original cost to be kept in a system of accounting may not be prescribed. Section 220(a) authorized the Commission in its discretion to "prescribe the forms of any and all accounts, records and memorandum to be kept by the carrier". The powers conferred by § 213(c) are not restrictive of § 220(a) nor does the latter section restrict the former. The two sections are capable of complementary treatment.

The requirement that original cost be set forth in accounting records of the telephone companies serves to complete the picture of value in revealing the property's financial background and showing the relationship of a carrier's monetary return to the original as well as to its own investment. It aids the Commission in its duty to determine from all the pertinent circumstances and factors, the just and reasonable rates which the carrier may exact from its service. Original cost is a relevant factor. Smyth v. Ames, 169 U. S. 466, 547; Los Angeles Co. v. R. R. Comm., 289 U. S. 287, 306, cf. § 213(a) of the Act. The object of the system of accounts might well be to display the pertinent financial operation and throw light upon its present condition. Kansas City Southern Ry. v. U. S., supra, at p. 440. Original cost as a segregated item on a balance sheet may serve to reveal actualities which may be pertinent in fixing a rate base on the capitalized earning power of a property [fol. 754] purchased. In making readily available facts which would tend to expose discrepancies in valuation, it cannot be said the system is so arbitrary as to be beyond the commission's power. Forty-seven state public utility bodies acquiesce in the proposed requirements. This is not evidence of unreasonableness.

The new system requires that when telephone plant in service is acquired, the amount paid therefor shall be charged to account 276 (Telephone plant acquired). The original cost of the property, estimated if not known, shall then be charged (debited) to the appropriate telephone plant account, whether "in service" (100.1), "under construction" (100.2), or "held for future use" (100.3) and credited to account 276. After debits to 276 for "contributions", and for reserve requirements for depreciation and amortization to date of the plant acquired, the amount remaining in 276 shall be debited or credited as appropriated to account 100.4 (Telephone plant acquisition adjustment).

As to 100.4, the system provides: "The amounts recorded in this account with respect to each property acquisition shall be disposed of, written off, or provision shall be made for the amortization thereof in such manner as this Commission may direct [100.4(c)]." "Original cost" as used is defined as "the actual money cost of or the current money value of any consideration other than money exchanged for property at the time when it was first dedicated to the public use, whether by the accounting company or by a predecessor public utility" (instruction 3-S-1).

The plaintiffs direct at this requirement the objection that these provisions violate the fundamental principles [fol. 755] of accounting in the following respects: although 100.1, 100.2, 100.3 and 100.4 if added together immediately will show the company's actual investment in its plant, since 100.4 must be written off at the will of the Commission, it will be necessary to carry a surplus reserve against this possible write-off. Once the write-off has been made, they declare that no combination of balances will reflect the company's actual investment. And they object further, because there can be no depreciation charge to any amount in account 100.4.

In considering the merits of these objections, it becomes necessary to examine, for purposes of comparison, the system now in effect which the plaintiffs do not attack as unreasonable and which they seek to retain. Under the present system, account 278 "undistributed cost of property" performs a function similar to account 100.4. Under it, when a purchase is made, the estimated current value of the land, the current cost new (estimated if not known) of certain other telephone plant, the original cost of franchises, and the cost of uncompleted projects are charged to their corresponding accounts. After crediting to reserve accounts, the estimated depreciation and amortization applicable, the difference between the total of the foregoing amounts and the cost to the accounting company of the plant acquired is debited or credited to 278, "undistributed cost of property". Account 278 is classed as a "telephone plant account" and is reported in the balance sheet as part of account 100 (Telephone plant).

As an alternative, the Commission may permit the transfer of the amounts in the "telephone plant accounts" [fol. 756] and in "depreciation and amortization reserve

accounts" as carried in the books of the vendor company to the books of the purchaser. In some instances, the amounts actually paid by the purchasing companies have been recorded in the "plant" accounts. Thus, actual cost, current cost new at the time of purchase, and original cost at the time of first dedication are in use at present as the basis of various telephone plant accounts. The amount in 278 of the present system is subject to no depreciation and may be written off only through surplus.

On a comparison of the two systems, that of this Commission seems to more accurately reflect the condition and record the history of the plant. Account 100.4 is listed among investments. It can be subdivided so that there can be segregated any amount therein not representing (1) the cost of elimination of competition; (2) payment to an affiliate at a price in excess of cost to it with a profit returnable to the purchasing company in the form of dividends or otherwise; and (3) any other element not expended in public interest.

This segregated amount would receive the same treatment substantially in the rate and depreciation basis as would amounts appearing in 100.1 "Telephone plant in service". In this light, it appears that the proposed system merely provides segregation, and that the addition of the amounts in these investment accounts 100.1 through 100.4 would accurately picture the legitimate investments of the purchasing company.

[fol. 757] To follow the plaintiffs in their argument that a reserve of surplus must be maintained against 100.4 and that this is fundamentally wrong, would be to ignore the similarity between 278 of the present system and 100.4 of the proposed system, and further it requires the assumption that the Commission will act improperly in the future under 100.4(c). This cannot be presumed. The order provides for alternatives adaptable to the facts of individual cases. This flexibility distinguishes the system at bar from that held invalid in New York Edison Co. v. Maltbie (344 A. D. (N. Y.) 685). This cannot be held, before any order under 100.4(c) has been made by the Commission, to be such an arbitrary method of accounting that the order imposing it is void.

The same argument applies to the objection that no depreciation is allowed against item 100.4 "acquisition adjustments". This complaint anticipates arbitrary action

by the Commission, under 100.4(c) which authorizes handling of this item through amortization. The effect would be the same as writing down through depreciation, and until the Commission acts so that the accounts become so contrary to the principles of correct accounting as to constitute the Commission's order arbitrary and unreasonable, the Commission is within its powers. The court need not agree the accounting proposed is the best method, but at this stage it cannot be said the provision is arbitrary. The objection is made that the Commission's refusal to act properly within 100.4(c) would constitute a negative order, non-reviewable within the doctrine of Proctor & Gamble v. [fol. 758] United States, 225 U. S. 282. This would not cut off the plaintiff's right of attacking the system as it would apply to them after such a refusal. The appeal need not be on the order denying relief but can be against the system as its operation is affected by such denial.

There is no deprivation of property involved here. The Supreme Court has noted that the question merely concerned accounting and that there was no occasion to hold the order invalid as a deprivation of property until actual damage was threatened by it as in the use of an improper rate base in setting rates. Norfolk & Western Ry. Co. v. United States, 287 U. S. 134; United States v. Los Angeles & Salt Lake R.R. Co., 273 U. S. 299.

The plaintiffs object that no depreciation is allowed on property held for future use in account 100.3. Except in those rare instances when the entire cost of depreciation covers only the wear and tear on equipment in use, the plant held in reserve will depreciate because of obsolescence or deterioration as it is not entirely dependent on use. The exclusion of depreciation on this account as an item to be considered in rate determinations may be supportable but it appears unjustifiable to bar depreciation on this item altogether. Where the property is withdrawn from service for any portion of its life, upon its final retirement, the depreciation reserve set up for it would be inadequate. This can be adjusted by charging the depreciation to surplus rather than as a current account. Thus a true reflection of the adjusted value of the property would be obtained, and yet the accounts will so set off the item that it

may be excluded from consideration as a current expense [fol. 759] for rate purposes.

Instruction 21(B)(3) directs a purchaser of property which has been acquired by the prior owner as a contribution, to record the contribution which the seller had received. This is done by crediting account 175 "contributions of telephone plant" and debiting the same amount on the asset side, to account 100.4 "Telephone plant acquisition and adjustment" [Instruction 21(B)(4)]. Since this requirement is in addition to the usual entries covering the purchase, it results in swelling the assets and liabilities by a fictitious entry. It constitutes a double recording of this portion of the transaction. This part of the property is recorded once in the usual record of the transaction, and to require its inclusion a second time is unreasonable. No sufficient reason is advanced for such treatment. The desired record could be made without this inflation by a subdivision of account 100.4. It is unreasonable to require duplication and the plaintiffs are injured in so far as they are denied a reasonable and true accounting record by this provision.

Instruction 2(b)(1) is also objected to.

It provides:

"All charges to the accounts prescribed in this classification for telephone plant, income operating revenues, and operating expenses, shall be just and reasonable and any payment by the company in excess of such just and reasonable charges shall be included in account 323 Miscellaneous income charges."

The information this requirement makes available is essential to any determination of reasonable rates within 201(b) of the Act. [ch. 1(4-5) of the Interstate *within 201(b)* [fol. 760] *of the Act* [*ch. 1(4-5) of the Interstate* Commerce Act) since they are directly affected by such charges. In the present system, instruction 22 (10)(a) stipulates that the telephone plant accounts be charged with "reasonable amounts for interest during construction period". The concept is no more indefinite there than the one more widely applied in the proposed system. The idea of "reasonable" is old in the fixation of public utility rates and every rate determination involves consideration of charges here made subject to a distinction between reasonable and

unreasonable. Although in isolated cases the question may be very close, generally the classification will not be impossible. As an accounting measure merely, the rule cannot be regarded as beyond the Commission's power.

Exception is also taken to the rule as requiring obedience to a standard as vague and indefinite as to be unconstitutional within the doctrine announced in United States v. Cohen Grocery (255 U. S. 81), Tedrow v. Lewis & Son Co., (255 U. S. 98) and A. B. Small Co. v. American Sugar Refining Co. (267 U. S. 233). First, it appears that the requirement that profits on transactions involving necessaries should not be unjust or unreasonable is without the specialized content of the word "reasonable" with regard to charges involved in the determination of rates. This serves to distinguish the plaintiff's other cases. cf. Connally v. General Construction Co., 264 U. S. 385; Cline v. Trink Dairy Co., 274 U. S. 445; Champlin Refining Co. v. Oklahoma Corp. Commission, 286 U. S. 210.

[fol. 761] Second, telephone companies need incur no risk since those occasional cases which may be doubtful can be submitted for approval under §220(g) of the act and instruction 9 of the order. To the claim that the Commission is likewise without a standard for judgment, the answer is that the concept of "reasonable" is traditionally defined in utility regulation with sufficient certainty.

The necessity of this order becomes apparent upon consideration of the interrelations of telephone companies. License agreements between subsidiaries can furnish examples of charges clearly not "just and reasonable". Yet any exact definition would be objectionable as arbitrary.

Furthermore, these items, in being subject to interpretation by the Commission and definition as applied to specific facts, are sufficiently definite to guide the Commission. Cf. Pennsylvania Co. v. United States, 236 U. S. 351, 361; Interstate Commerce Comm. v. Alabama Midland Ry., 168 U. S. 144, 170.

It is required that the capital stock expense be set up in account 134.2 which falls in the general class of "prepaid Accounts and Deferred Charges". 134.2(c) provides that the amortization of this account shall be accomplished by charges to "Miscellaneous debits to surplus". Instruction 20(a) states that the telephone plant accounts, 201-277, shall include the general expense of organization of the ac-

counting company. While the system may appear to be inconsistent in this respect, Montgomery, Auditing Theory & Practice [5th Ed. 1934] p. 416, endorses the write-off of organization expenses to charges against earned surplus, [fol. 762] and this would be not unreasonable in view of the accountant's differences on the point. See, Paton Accountant's Handbook [2nd Ed. 1934] p. 42.

If inconsistency exists, it may be corrected by the Commission before this requirement can be enforced. What we say must not be regarded as an endorsement of the indiscriminate exclusion of these expenses from the rate base. See: Ohio Utilities v. Pacific Utilities Comm., 267 U. S. 359. Nor does it mean that expenses of stock flotations subsequent to organization are always necessarily to be regarded as organization expenses.

Except as indicated herein in connection with the depreciation for plant and equipment held for future use, and contributions, the injunction herein prayed for must be denied, but a decree will be entered restraining the enforcement of the instructions given as to these two items.

A decree for plaintiffs as limited in this opinion, may be entered.

February 18, 1936.

Martin T. Manton, Circuit Judge. Augustus N. Hand, Circuit Judge. Jno. C. Knox, District Judge.

[fol. 763] In United States District Court

[Title omitted]

Findings of Fact and Conclusions of Law—Filed March 24, 1936

This cause came on regularly to be heard before underscribed Martin T. Manton and Augustus N. Hand, Circuit Judges, and John C. Knox, District Judge, sitting as a statutory three-judge court, on the 13th and 14th days of December, 1935, at New York City, New York, pursuant to Orders to Show Cause herein, which issued upon the application of the several plaintiffs for an interlocutory injunction suspending, during the pendency of said cause, the operation of Telephone Division Order No. 7-C of the Federal Com-

munications Commission, dated June 19, 1935, prescribing the Uniform System of Accounts for Telephone Companies, Issue of June 19, 1935, effective January 1, 1936, and for a temporary stay of the operation of said order pending the determination of said application for an interlocutory injunction; and the cause having been fully argued by counsel; and the parties having stipulated in open court to submit said cause for final determination upon the pleadings, affidavits and briefs on file, and to be filed as then directed by this Court; and this Court having heretofore made an Order for a Temporary Stay by the terms of which the operation of Telephone Division Order No. 7-C was stayed and suspended until the final decree or further order of this Court; and the affidavits and briefs of the parties having been filed as directed; and this Court having been fully [fol. 764] advised in the premises, and an opinion in writing having been delivered by Judge Manton, Judges Hand and Knox concurring, this Court, pursuant to Federal Equity Rule 70½, now makes the following:

Findings of Fact

I

The allegations and admissions set forth in Sections 1 to 5 of the Bill of Complaint of original plaintiffs, the allegations and admissions set forth in Sections 1 to 7 of the Bill of Complaint of additional plaintiffs, the allegations and admissions set forth in Sections 1 to 6 of the Bill of Intervention of intervening plaintiffs, and the answers of the United States of America and of the Federal Communications Commission to said respective sections of said Bills of Complaint and said Bill of Intervention (which are largely pro forma) are true.

All references hereinafter made to "plaintiffs" shall include the original plaintiffs, the additional plaintiffs, and the intervening plaintiffs.

II

Telephone Division Order No. 7-C was prescribed by the defendant Federal Communications Commission, after extensive preliminary work and conferences, pursuant to the authority granted in Section 220 of the Communications Act of 1934, and the conclusions of the Commission are set forth

in said order. Forty-seven state public utility regulatory bodies acquiesce in the proposed requirements.

III

Telephone Division Order No. 7-C requires plaintiffs to include in the telephone plant accounts the "original cost" of their telephone plant, and provides that the difference between said original cost and cost to the accounting company of property acquired from another public utility shall be recorded on their books in other specified investment accounts.

IV

Plaintiffs have heretofore performed accounting with respect to property acquired from other public utilities which resulted in the inclusion in their telephone plant accounts of amounts representing various costs, such as current cost [fol. 765] new, actual cost to plaintiffs, structural value, or cost to the predecessor company (by merger of book accounts). The Uniform System of Accounts prescribed by Telephone Division Order No. 7-C requires that in accounting for property acquired from another public utility, and in all other instances, plaintiffs' telephone plant accounts shall be stated on a uniform basis, that being "original cost", as therein defined.

V

Telephone Division Order No. 7-C does not require that the recorded cost or investment of the plaintiffs in property theretofore acquired by them from another public utility be obliterated or eliminated from their investment accounts, but merely requires plaintiffs to segregate the element of recorded cost or investment into the following investment accounts:

100.1 Telephone plant in service.
100.2 Telephone plant under construction.
100.3 Property held for future telephone use.
100.4 Telephone plant acquisition adjustment.

VI

Telephone Division Order No. 7-C further requires plaintiffs to include in their investment accounts the amount

which they actually pay for property acquired on and after January 1, 1936, from other public utilities.

VII

Telephone Division Order No. 7-C requires plaintiffs to segregate in an account numbered 100.4 and entitled "Telephone plant acquisition adjustment", the difference between (a) the amount of money which they actually paid for telephone plant acquired and (b) the original cost of such plant less the amounts of reserve requirements for depreciation and amortization of the property acquired and amounts of contributions to the predecessor company or companies for the construction and acquisition of such property.

VIII

The plaintiffs are not prevented by Telephone Division Order No. 7-C from recovering amounts included in Account 100.4 in view of the alternative provisions of paragraph (C) of the text of said Account 100.4, which make provision for the amortization or other appropriate disposition of amounts included in Account 100.4. The Commis- [fol. 766] sion has made no direction with respect to the disposition of any such amounts.

IX

Telephone Division Order No. 7-C requires that plaintiffs' accounts shall be kept on a basis which will reflect the facts with respect to their transactions and which will show their actual condition for the information of all persons interested therein, except with respect to contributions to predecessor utilities and depreciation of property held for future telephone use, and said order is capable of practical application except with respect to contributions to predecessor utilities.

X

Telephone Division Order No. 7-C does not prevent plaintiffs from recording in their expense accounts the expense of depreciation which they actually incur, except that said order does not provide for depreciation of the classes of depreciable property, the original cost of which is includible in Account 100.3, "Property held for future telephone use".

XI

Telephone Division Order No. 7-C does not require plaintiffs to write off any portion of their actual investment where they have paid a price in excess of original cost, but merely requires a segregation of this actual cost into certain investment accounts, all of which will appear in the balance-sheet statements of plaintiffs; and no writing off is required by the provisions of Order No. 7-C when plaintiffs purchase property in the future, but only a segregation of such cost is required.

XII

Telephone Division Order No. 7-C does not require plaintiffs to make radical or retroactive changes in their completed accounts. In this respect said order merely requires the reclassification of balances as of its effective date in certain balance-sheet accounts.

XIII

Telephone Division Order No. 7-C does not require that amounts recorded in Account 100.4 be disposed of, written off, or amortized by plaintiffs. The form of the accounting [fol. 767] to be performed is dependent upon the development of facts in connection with each individual acquisition. Said order merely provides for alternative modes of disposition adaptable to the facts of individual acquisitions.

XIV

Plaintiffs are required to record in Account 175 "Contributions of telephone plant", on the "liability side" of the balance sheet and in Account 100.4, "Telephone plant acquisition adjustment", on the "asset side" of the balance sheet, the amounts of contributions made to other public utilities with respect to property subsequently acquired by the accounting company. This requirement is in addition to the usual entries for the purchase of property and results in increasing the statement of both the assets and liabilities in equal amount. It constitutes a double recording of this portion of the transaction.

XV

The distinctions between Accounts 100.1, 100.3 and 103, and the respective amounts includible therein, are suffi-

ciently clear and definite from the titles and texts of the accounts, and instructions relating thereto, to be understood readily by those charged with the duty of keeping said accounts.

XVI

Telephone Division Order No. 7-C does not require that the original cost of plaintiffs' necessary space plant shall be included in Account 100.3 but that such cost shall be included in Account 100.1, "Telephone plant in service." Plaintiffs are permitted to recover the full expense of depreciation of property, the original cost of which is includible in said Account 100.1.

XVII

The requirement that charges to the telephone plant, income, operating revenue, and operating expense accounts shall be just and reasonable, and that any payments in excess of such just and reasonable charges shall be charged to Account 323, "Miscellaneous income charges", is essential to any determination of reasonable rates. Instruction 22 (B) (10) (a) of the accounting system heretofore prescribed by the Interstate Commerce Commission stipulates that the telephone plant accounts shall be charged with [fol. 768] "reasonable amounts for interest during the construction period". The concept is no more indefinite there than the one more widely applied in the proposed system. The idea of "reasonable" is old in the fixation of public utility rates and every rate determination involves consideration of charges here made subject to a distinction between reasonable and unreasonable. Although in isolated cases the question may be very close, generally the classification will not be impracticable. As an accounting measure, Instruction 2 (B. 1) of Telephone Division Order No. 7-C cannot be regarded as arbitrary or unreasonable. The standard contemplated by said instruction is neither vague nor indefinite.

XVIII

Telephone Division Order No. 7-C constitutes a complete system of accounts for telephone companies but the provisions therein complained of are separable.

XIX

Telephone Division Order No. 7-C does not require plaintiffs to keep, during the year 1936, almost a complete set of accounts in accordance with the present system in addition to a complete set of accounts in accordance with the system prescribed by said order. The order requires that certain accounts, few in number, shall be kept for a period of only one year so as to preserve their continuity and to permit comparison with the accounts of prior years. Compliance with said requirements is not unduly burdensome nor expensive, neither is it arbitrary or unreasonable.

XX

The provisions of Telephone Division Order No. 7-C which require that capital stock expense be included in Account 134.2, "Capital stock expense," and that the amounts in this account may be written off or amortized only through surplus are recognized by accounting authorities as sound and appropriate accounting.

XXI

The provisions of Telephone Division Order No. 7-C which require that the cost of repairs of outside plant (for Class A companies) shall be recorded in separate operating expense accounts are recognized by accounting authorities as sound and appropriate accounting.

[fol. 769] From the foregoing Facts, the Court makes the following:

Conclusions of Law

I

Each and all of the several plaintiffs herein are telephone carriers subject to the Communications Act of 1934. This Court has jurisdiction of the action and of all parties thereto. Plaintiffs have no adequate remedy at law. They have not been guilty of laches and they are entitled to maintain this suit.

II

Section 220(a) of the Communications Act of 1934 empowers the Federal Communications Commission in its discretion to prescribe the forms of any and all accounts to

be kept by carriers subject to said Act. Section 404 of the Act requires that said Commission shall make a report in writing with respect to its investigations and requires findings of fact to be included only in case damages are awarded. Said section does not render invalid orders made pursuant to Section 220(a) of the Act which are unaccompanied by such reports or by findings of fact. Telephone Division Order No. 7-C is an administrative order made pursuant to Section 220(a) of the Act. Said order prescribes a uniform system of accounts for carriers subject to the Act. It does not award damages and no report or findings of fact are required as a condition to its validity. The conclusions of said Commission, however, are very evident from the order itself.

III

Under Section 220(a) of the Communications Act of 1934 the Federal Communications Commission is empowered to prescribe a uniform system of accounts and it may lawfully require that the telephone plant accounts be kept on an original cost basis. Section 213(c) of said Act authorizes said Commission to obtain from telephone carriers at any time information concerning the original cost of their properties. Section 219(a) of said Act authorizes said Commission to require annual reports from said carriers and to prescribe the forms thereof. However, the powers conferred upon said Commission by Sections 213(c) and 219 (a) of said Act are not restrictive of the powers conferred under Section 220(a) thereof. The former sections do not restrict the latter section, and all are capable of complementary treatment.

[fol. 770]

IV

Plaintiffs are not deprived of their property without due process of law in violation of the Fifth Amendment to the Federal Constitution by the provisions of Telephone Division Order No. 7-C which require them to include in their telephone plant accounts the original cost of their telephone plant, and which further require that the difference between said original cost and the cost to the accounting company of property acquired from another public utility shall be recorded on their books in other specified investment accounts. Said provisions serve to complete the picture of

value in revealing the financial background of the property and showing the relationship of a carrier's monetary return to the original cost as well as to its own investment. It is the duty of the Federal Communications Commission to determine from all circumstances and factors the just and reasonable rates which a carrier may exact for its services. The original cost is a relevant factor, the recordation of which assists the Commission in the performance of its duty. The recordation of such original cost as a segregated item on the balance sheet may serve to reveal actualities which may be pertinent in connection with valuation for rate making purposes, passing upon security issues, depreciation accounting and other regulatory functions. The provisions of Telephone Division Order No. 7-C relating to the recordation of original cost as a segregated item are not arbitrary or unreasonable and they are within the power of said Commission to prescribe.

V

The provisions of Telephone Division Order No. 7-C, which require that plaintiffs shall segregate the element of recorded cost or investment in property acquired from another public utility into the following investment accounts:

100.1 Telephone plant in service.
100.2 Telephone plant under construction.
100.3 Property held for future telephone use.
100.4 Telephone plant acquisition adjustment.

do not deprive plaintiffs of their property without due process of law, and said requirements are not arbitrary or unreasonable, and they are within the power of the Federal Communications Commission to prescribe.

[fol. 771]

VI

The provisions of paragraph (C) under Account 100.4 of Telephone Division Order No. 7-C, which relate to the alternative modes of disposition to be made of amounts includible in said Account, do not operate to deprive plaintiffs of their property without due process of law, and they are not arbitrary or unreasonable, and they are within the power of the Federal Communications Commission to prescribe.

VII

Instruction 2 (B.1) of Telephone Division Order No. 7-C is neither vague nor indefinite in its provisions. Said instruction does not contravene the Sixth Amendment to the Federal Constitution, and it does not operate to deprive plaintiffs of their property without due process of law, and it is not arbitrary or unreasonable, and it is within the power of the Federal Communications Commission to prescribe.

VIII

The provisions of Account 134.2 of Telephone Division Order No. 7-C do not operate to deprive plaintiffs of their property without due process of law, and they are not unreasonable or arbitrary, and they are within the power of the Federal Communications Commission to prescribe.

IX

The provisions of Accounts 602.1 to 602.9, inclusive, and 603, of Telephone Division Order No. 7-C, which require the recordation therein of the cost of repairs of outside plant (for Class A companies), do not operate to deprive plaintiffs of their property without due process of law, and they are not arbitrary or unreasonable, and they are all within the power of the Federal Communications Commission to prescribe.

X

The failure of Telephone Division Order No. 7-C to make specific provision for depreciation of the classes of depreciable property, the original cost of which is includible in Account 100.3, "Property held for future telephone use", is unjustifiable. Such depreciation should not be denied for the time the original cost thereof is includible in said Account 100.3.

[fol. 772]

XI

Instruction 21 (B) (3) of Telephone Division Order No. 7-C pertains to contributions to predecessor utilities. Said instruction prevents plaintiffs from keeping a reasonable and true accounting record and is injurious to plaintiffs

and, therefore, unreasonable, and should be eliminated from said Uniform System of Accounts.

XII

The requirement of the fourth ordering clause of Telephone Division Order No. 7-C that plaintiffs keep certain additional accounts during the year 1936 does not deprive plaintiffs of their property without due process of law, and it is a reasonable and legal requirement within the power of the Federal Communications Commission to prescribe.

XIII

Telephone Division Order No. 7-C is not retroactive in its requirements.

XIV

Telephone Division Order No. 7-C constitutes a complete system of accounts, but the provisions thereof are separable, and said system of accounts is capable of practical application, notwithstanding the elimination of Instruction 21 (B) (3) therefrom. Said Uniform System of Accounts makes adequate provision for the accurate recordation of the facts of plaintiffs' transactions and the true reflection of their actual condition, and said system is reasonable, and is in accord with sound principles of accounting, and is within the power of the Federal Communications Commission to prescribe, provided that plaintiffs are not prevented from accounting for depreciation of the classes of depreciable property for the time the original cost of such property is includible in Account 100.3.

XV

Plaintiffs are entitled to a decree vacating, setting aside, and annulling Instruction 21 (B) (3) of Telephone Division Order No. 7-C, and enjoining the Federal Communications Commission from preventing the plaintiffs, or any of them, from accounting for depreciation of the classes of depreciable property for the time the original cost of such property is includible in Account 100.3, "Property held for [fol. 773] future telephone use". Plaintiffs are not entitled to any further equitable relief. The Order for Temporary Stay heretofore entered should be dissolved, and plaintiffs'

application for a permanent injunction and other relief should be denied in all other respects.

Dated this 24th day of March, 1936.

Martin T. Manton, Circuit Judge. Augustus N. Hand, Circuit Judge. John C. Knox, District Judge.

[fol. 774] IN UNITED STATES DISTRICT COURT

[Title omitted]

ADDITIONAL FINDINGS OF FACT—Filed March 26, 1936

1. The greater part of the properties of each of these additional plaintiffs was acquired by it from predecessor owners who in turn, in many cases, had acquired such properties from still other predecessor owners since the properties were first dedicated to the public use. There were at least 233 of such owners prior to said seven additional plaintiffs.

2. The greater part of the properties so acquired from predecessor owners by these additional plaintiffs, which is now in existence, has been recorded in their property investment accounts at its actual cost to these plaintiffs either in cash or in securities. Such property is of substantial value.

[fol. 775] 3. The former owners at the time when the telephone properties which were acquired by the additional plaintiffs from predecessors were first dedicated to the public use, consisted of small companies or individuals and in many cases, farmers' mutual associations.

4. The records of the immediate predecessors of additional plaintiffs were in almost every case incomplete and inaccurately kept, and were themselves in turn based on purchases of going businesses from their predecessors. In many cases no records at all were kept by the companies or individuals or farmers' mutual associations, who first dedicated them to the public use, and in many other cases their books and records are not now available and, if available, are known to be inaccurate.

5. The determination of the "original cost"; as defined in the system in suit*", of the properties acquired by the additional plaintiffs from predecessor owners would in numerous instances be a matter of estimate.

6. The cost to these additional plaintiffs of telephone properties acquired from predecessor owners has in most instances been approved by a state public service commission or other state agency at the time of acquisition.

7. The actual cost to these additional plaintiffs has been used as a basis for their financial operations, including the issuance of securities.

It is further noted that the defendants have taken an [fol. 776] exception to each of the above enumerated additional findings.

Dated March 25, 1936.

Martin T. Manton, Circuit Judge. Augustus N. Hand, Circuit Judge. Jno. C. Knox, District Judge.

[fol. 777] IN UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

In Equity. No. 81-366

AMERICAN TELEPHONE AND TELEGRAPH COMPANY, et al., Plaintiffs; Ohio Associated Telephone Company, et al., Additional Plaintiffs; Eastern Telephone and Telegraph Company, et al., Intervening Plaintiffs,

vs.

UNITED STATES OF AMERICA and FEDERAL COMMUNICATIONS COMMISSION, Defendants; National Association of Railroad and Utility Commissioners, Intervening Defendants

DECREE—Filed March 24, 1936

This cause came on regularly to be heard before underscribed Martin T. Manton and Augustus N. Hand, Circuit

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* "System in suit", whenever used herein, means Order No. 7-C and the Uniform System of Accounts prescribed thereby, as found in the Issue of June 19, 1935.

Judges, and John C. Knox, District Judge, sitting as a statutory three-judge court, on the 13th and 14th days of December, 1935, at New York City, New York, pursuant to Orders to Show Cause herein, which issued upon the application of the several plaintiffs for an interlocutory injunction suspending, during the pendency of said cause, the operation of Telephone Division Order No. 7-C of the Federal Communications Commission, dated June 19, 1935, prescribing the Uniform System of Accounts for Telephone Companies, Issue of June 19, 1935, effective January 1, 1936, and for a temporary stay of the operation of said order pending the determination of said application for an interlocutory injunction; and the cause having been fully argued by counsel; and the parties having stipulated in open court to submit said cause for final determination upon the pleadings, affidavits, and briefs on file, and to be filed as then directed by this Court; and this Court having heretofore made an Order for a Temporary Stay by the terms of which the operation of Telephone Division Order No. 7-C was stayed and suspended until the final decree or further order of this Court; and the affidavits and briefs of the parties having been filed as directed; and this Court having been fully advised in the premises, and an opinion [fol. 778] in writing having been delivered by Judge Manton, Judges Hand and Knox concurring, and this Court having made and filed herein its Findings of Fact and Conclusions of Law.

Now therefore it is ordered, adjudged and decreed as follows:

1. The Federal Communications Commission is hereby enjoined from preventing the plaintiffs or any of them from accounting for depreciation of the classes of depreciable property, for the time the original cost of such property is includible in Account 100.3, "Property held for future telephone use" of the Uniform System of Accounts prescribed by Telephone Division Order No. 7-C;

2. The Federal Communications Commission is hereby enjoined from applying and enforcing the provisions of Instruction 21 (B) (3) of Telephone Division Order No. 7-C respecting contributions to the predecessor company or companies, and that part of paragraph (A) of the text of Account 100.4, "Telephone plant acquisition adjustment", which reads, "and amounts of contributions to the

predecessor company or companies for construction and acquisition of such property"; and said provisions are hereby declared null and void;

3. The Order for Temporary Stay entered herein on the 27th day of December, 1935, is hereby dissolved and plaintiffs' application for a permanent injunction is denied except as hereinabove provided; and plaintiffs are directed to comply with the provisions of said Telephone Division Order No. 7-C, as of January 1, 1936, except with respect to the two items hereinabove enjoined.

It is further ordered, adjudged and decreed that the written objections and exceptions of the plaintiffs and of the [fol. 779] defendants to the Findings of Fact, Conclusions of Law, and to this decree, be and they are hereby overruled; to which rulings plaintiffs and defendants respectively duly excepted.

Dated this 24th day of March, 1936.

(Sgd.) Martin T. Manton, Circuit Judge. (Sgd.) Augustus N. Hand, Circuit Judge. (Sgd.) John C. Knox, District Judge.

[fol. 780] In United States District Court

[Title omitted]

Petition for Appeal—Filed April 6, 1936

To the Honorable Martin T. Manton, Circuit Judge for the Second Circuit; Augustus N. Hand, Circuit Judge for the Second Circuit; John C. Knox, District Judge for the said District:

Come now plaintiffs, intervening plaintiffs and additional plaintiffs, and hereby appeal to the Supreme Court of the United States from the final decree made and entered herein on the 24th day of March, 1936, because of errors prejudicial to plaintiffs, intervening plaintiffs and additional plaintiffs, which are set forth in the assignment of errors presented and filed herewith. There is also presented and filed herewith a statement of the basis of jurisdiction of the Supreme Court of the United States States [fol. 781] to review said decree upon appeal.

Your petitioners respectfully pray that said appeal be allowed for the correction of the errors so complained of, and for the reversal of the decree in so far as it fails to grant the relief prayed for by plaintiffs, intervening plaintiffs and additional plaintiffs in their Bills of Complaint, that the amount of bond be fixed, that citation be issued as provided by law, and that a transcript of the record, duly authenticated, be sent to the Supreme Court of the United States, in accordance with the rules of that Court.

Dated, New York, N. Y., April 4, 1936.

C. M. Bracelen, Chas. T. Russell, Edward L. Blackman, Alan J. McBean, Solicitors for Plaintiffs and Intervening Plaintiffs. Allen T. Klots, Hayden N. Smith, Solicitors for Additional Plaintiffs.

[fol. 782] IN UNITED STATES DISTRICT COURT

[Title omitted]

ASSIGNMENTS OF ERROR—Filed April 6, 1936

Come now the plaintiffs, additional plaintiffs and intervening plaintiffs, hereinafter referred to as plaintiffs, and assign as errors upon which they will rely upon their appeal to the Supreme Court of the United States from the final decree of this court entered March 24, 1936, which final decree, with two exceptions therein specified, denied plaintiffs' application for a permanent injunction against the provisions of Telephone Division Order No. 7-C of the Federal Communications Commission and the system of accounts prescribed thereby, the following:

[fol. 783] The District Court erred:

1. In holding that the "original cost" provisions of said system (particularly Instructions 3 (S.1), 20 and 21, and Accounts 100.1, 100.2, 100.3, 100.4 and 202 to 277, inclusive), are not arbitrary or unreasonable, are within the power of the Commission to prescribe, do not deprive plaintiffs of their property without due process of law in violation of the Fifth Amendment to the Constitution of the United States and are valid, as against each of the following contentions of plaintiffs:

(a) That said provisions require the property investment accounts of plaintiffs to be kept so as to reflect, in the case of purchased property, not the actual investment of plaintiffs in such property, but the investment, estimated if not known, of the public utility first dedicating the property to the public use, thus causing the accounts of plaintiffs to conceal relevant facts as to their financial condition and to misrepresent such condition, all of which is contrary to the fundamental principles of correct accounting.

(b) That said provisions require that where plaintiffs have purchased or shall purchase property at a price higher than its cost to the predecessor utility which first dedicated it to the public use, they shall eliminate a part of their ac- [fol. 784] tual investment from their property investment accounts and place it in an account (Account 100.4) which, while listed among the investment accounts, is in actuality a suspense account which is subject to instant and total writing off at the will of the Commission, all of which amounts to requiring plaintiffs to record a loss on their books when in fact they have suffered no loss, and is contrary to the fundamental principles of correct accounting.

(c) That the disposition to which the items in Account 100.4 are made subject by paragraph C thereof imposes on these items implications which have no relation to the genesis of the items themselves.

(d) That said provisions, in effect, require plaintiffs to make retroactive changes in accounts which have been lawfully and correctly kept.

(e) That said provisions will cause plaintiffs great and useless expense, and will serve no useful purpose except the recording of information which could be obtained and recorded in supplementary statements at relatively minor expense and without causing the accounts of plaintiffs to misrepresent the facts.

2. In refusing to hold that the provisions referred to in Assignment of Error No. 1 are so arbitrary and unreason- [fol. 785] able as to constitute an abuse of the Commission's power, are beyond its authority, deprive plaintiffs of their property without due process of law in violation of the Fifth Amendment to the Constitution of the United States and are illegal and void, as against each of the contentions of plaintiffs specified in said assignment.

3. In refusing to set aside, annul and enjoin permanently the provisions referred to in Assignment of Error No. 1.

4. In holding that said order and system do not prevent plaintiffs from recording in their expense accounts the expense of depreciation which they actually incur with respect to the portion of their investment in depreciable property recorded in Account 100.4 and that in this respect said order and system are valid.

5. In refusing to hold that said order and system, in excluding from the provisions for depreciation accounting any provision for recording the expense of depreciation with respect to the portion of plaintiffs' investment in depreciable property recorded in Account 100.4, prevent plaintiffs from recording in their accounts the expense of depreciation which they actually incur, and that in this respect [fol. 786] said system is contrary to the fundamental principles of correct accounting, is so arbitrary and unreasonable as to constitute an abuse of the Commission's power, is beyond its authority, deprives plaintiffs of their property without due process of law in violation of the Fifth Amendment to the Constitution of the United States, and is illegal and void.

6. In refusing to set aside, annul and enjoin permanently said order and system for the reasons specified in Assignments of Error Nos. 4 and 5.

7. In holding that the provision of paragraph (C) of Account 100.4 of said system that the portion of the investment recorded in said account with respect to each property acquistion shall be disposed of, written off or amortized, not in accordance with any rule or classification contained in said accounting system or elsewhere, but as the Commission may in each instance direct, is not arbitrary or unreasonable, and is within the power of the Commission to prescribe.

8. In refusing to hold that the provision specified in Assignment of Error No. 7 is arbitrary and unreasonable, beyond the authority of the Commission, illegal and void.

9. In refusing to set aside, annul and enjoin permanently the provision referred to in Assignments of Error Nos. [fol. 787] 7 and 8 for the reasons specified in said assignments.

10. In holding that Instruction 2 (B.1) of said system is essential to any determination of reasonable rates, is not contrary to the fundamental principles of correct accounting, is not arbitrary or unreasonable and is within the power of the Commission to prescribe.

11. In refusing to hold that Instruction 2 (B.1) of said system is contrary to the fundamental principles of correct accounting, unreasonable, arbitrary, beyond the authority of the Commission to prescribe, illegal and void.

12. In holding that Instruction 2 (B.1) of said system is neither vague nor indefinite and that it does not deprive plaintiffs of their property without due process of law in violation of their rights under the Fifth Amendment to the Constitution of the United States.

13. In refusing to hold that Instruction 2 (B.1) of said system lays down a rule which is so vague and indefinite as not to constitute a legal standard of conduct, that the enforcement thereof would violate the rights of plaintiffs to due process of law as guaranteed by the Fifth Amendment to the Constitution of the United States, and that said provision is void.

[fol. 788] 14. In refusing to set aside, annul and enjoin permanently Instruction 2 (B.1) of said system for the reasons specified in Assignments of Error Nos. 10, 11, 12 and 13.

15. In holding that the classification of property investment into Accounts 100.1, 100.3 and 103, as prescribed by said system, is not so vague as to be contrary to the fundamental principles of correct accounting, unreasonable or arbitrary, and is within the power of the Commission to prescribe.

16. In refusing to hold that the classification of property investment into Accounts 100.1, 100.3 and 103, as prescribed by said system, is so vague as to be contrary to the fundamental principles of correct accounting, arbitrary, unreasonable, beyond the authority of the Commission, illegal and void.

17. In holding that the distinctions between Accounts 100.1, 100.3 and 103 of said system are sufficiently clear and definite to be understood readily, and that this classification

does not deprive plaintiffs of their property without due process of law in violation of their rights under the Fifth Amendment to the Constitution of the United States.

18. In refusing to hold that the classification of property investment into Accounts 100.1, 100.3 and 103, as prescribed [fol. 789] by said system, lays down a rule which is so vague and indefinite as not to constitute a legal standard of conduct, that the enforcement thereof would violate the rights of plaintiffs to due process of law as guaranteed by the Fifth Amendment to the Constitution of the United States, and that said provision is void.

19. In refusing to set aside, annul and enjoin permanently said order and system for the reasons specified in Assignments of Error Nos. 15, 16, 17 and 18.

20. In holding that the provisions of said system complained of by plaintiffs are separable from said system of accounts as a whole.

21. In refusing to hold that without the provisions of said system specified in Assignments of Error Nos. 1 and 15 said system would be incomplete and would be no system at all unless other provisions were inserted in lieu thereof, that said provisions are non-severable, and that the system as a whole is therefore illegal and void because of the illegality of said provisions.

22. In refusing to set aside, annul and enjoin permanently said order and system for the reason stated in Assignment of Error No. 21.

23. In finding (Finding of Fact III) that said system requires the difference between "original cost" and cost [fol. 790] to the accounting company to be recorded in "other specified investment accounts." Account 100.4, in which such difference must be recorded, is not an investment account.

24. In finding (Finding of Fact V) that said order does not require that the recorded cost or investment of plaintiffs in property theretofore acquired by them from another public utility be eliminated from their investment accounts, but merely requires them to segregate such recorded cost or investment into investment accounts 100.1, 100.2, 100.3, and 100.4. Account 100.4 is not an investment account.

25. In finding (Finding of Fact VI) that said order requires plaintiffs to include in their investment accounts the amount which they actually pay for property acquired on and after January 1, 1936, from other public utilities. Account 100.4, in which a part of such actual payments must be included, is not an investment account, and the investment accounts will therefore include only a part of such actual payments.

26. In finding (Finding of Fact VIII) that plaintiffs are not prevented by said order from recovering amounts included in Account 100.4 in view of the provisions of paragraph (C) of the text of Account 100.4, which make provision for the amortization or other appropriate disposition of amounts included in Account 100.4. Said paragraph (C) [fol. 791] makes no provision for amortization or disposition unless the Commission shall make a further order, which it has not done.

27. In finding (Finding of Fact IX) that said order requires plaintiffs' accounts to be kept on a basis which will reflect the facts and which will show their actual condition, except with respect to contributions to predecessor utilities and depreciation of property held for future telephone use, and that said order is capable of practical application except with respect to contributions to predecessor utilities. (See Assignments Nos. 1 and 4.)

28. In finding (Finding of Fact X) that said order does not prevent plaintiffs from recording in their expense accounts the expense of depreciation which they actually incur, except that it does not provide for depreciation on depreciable property included in Account 100.3. (See Assignments Nos. 4 and 5.)

29. In finding (Finding of Fact XI) that said order does not require plaintiffs to write off any part of their present or future investment, but merely requires a segregation of their actual investment into certain investment accounts. Account 100.4, in which a part of their actual investment [fol. 792] must be segregated, is not an investment account but a suspense account subject to write-off at the direction of the Commission, and the segregation into this account is accomplished by writing it off from the investment accounts.

30. In finding (Finding of Fact XII) that said order does not require plaintiffs to make radical or retroactive changes in their completed accounts, but merely requires the reclassification of balances as of its effective date in certain balance sheet accounts. The required changing of all investment and telephone plant accounts to reflect the "original cost" of the property included therein in lieu of the prices actually paid and heretofore entered in the accounts is retroactive and radical change.

31. In finding (Finding of Fact XIII) that said order merely provides for alternative modes of disposition of the amounts recorded in Account 100.4, depending on the facts in connection with each individual acquisition. Said finding is contrary to the terms of said order, which include no reference to any such facts nor to any standard or rule which the facts in connection with such an individual transaction might make applicable and which make no provision for disposition of such amounts.

[fol. 793] 32. In finding (Finding of Fact XV) that the distinctions between Accounts 100.1, 100.3 and 103, and the respective amounts includible therein, are sufficiently clear and definite from the titles and texts of the accounts and instructions relating thereto to be understood readily by those charged with the duty of keeping the accounts.

33. In finding (Finding of Fact XVI) that said order does not require that the original cost of plaintiffs' necessary spare plant shall be included in Account 100.3 but that such cost shall be included in Account 100.1. Said order and system contain no provision, express or implied, as to what account shall include spare plant, necessary or otherwise.

34. In finding (Finding of Fact XVII) that Instruction 2 (B.1) of said system is essential to any determination of reasonable rates, that it is not impracticable of application, arbitrary or unreasonable and that the standard contemplated by said instruction is neither vague nor indefinite.

35. In finding (Finding of Fact XVIII) that the provisions of said order and system complained of by plaintiffs are separable.

Wherefore, plaintiffs, additional plaintiffs and intervening plaintiffs, and each of them, pray that the said decree be [fols. 794-820] reversed in so far as it fails to grant the re-

lief prayed for in their bills of complaint, and that the United States District Court for the Southern District of New York be ordered to enter a decree in accordance with the prayers of the bills of complaint, or in such other form as the Supreme Court of the United States may deem just.

C. M. Bracelen, Chas. T. Russell, Edward L. Blackman, Alan J. McBean, Solicitors for Plaintiffs and Intervening Plaintiffs. Allen T. Klots, Hayden N. Smith, Solicitors for Additional Plaintiffs.

[fol. 821] IN UNITED STATES DISTRICT COURT

[Title omitted]

ORDER ALLOWING APPEAL—Filed April 6, 1936

Upon the petition of plaintiffs, intervening plaintiffs and additional plaintiffs for the allowance of an appeal to the Supreme Court of the United States from the decree entered herein on March 24, 1936, assignment of errors and statement of the basis of jurisdiction of the Supreme Court being presented and filed therewith:

Ordered, that said appeal be, and the same is, hereby allowed as prayed.

It is Further Ordered, that bond on appeal, to be ap-
[fol. 822] proved by the Court, is fixed at the sum of $250.00.

It is Further Ordered that a transcript of the record, duly authenticated, be transmitted forthwith to the Supreme Court.

Dated April 4th, 1936.

Martin T. Manton, Circuit Judge. Augustus N. Hand, Circuit Judge. Jno. C. Knox, District Judge.

[fols. 823 & 824] Bond on appeal for $250.00, approved April 4, 1936, omitted in printing.

[fol. 825] IN UNITED STATES DISTRICT COURT

[Title omitted]

NOTICE OF APPEAL—Filed April 6, 1936

To the Honorable John C. Bennett, Attorney General of the State of New York:

Pursuant to the Urgent Deficiencies Appropriations Act of October 22, 1913, 38 Stat. 220, you are hereby notified that American Telephone and Telegraph Company, et al., plaintiffs, Ohio Associated Telephone Company, et. al., additional plaintiffs, and Eastern Telephone and Telegraph Company, et al., intervening plaintiffs herein have taken an appeal to the Supreme Court of the United States from the final decree of the United States District Court, entered March 24th, 1936, denying the prayer of said parties that [fol. 826] that certain order of the Federal Communications Commission designated "Telephone Division Order No. 7-C" prescribing a "Uniform System of Accounts for Telephone Companies, Issue of June 19, 1935, Effective January 1, 1936," be enjoined, set aside, and annulled; and the order allowing the said appeal makes the same returnable in the Supreme Court of the United States within forty days from the date hereof.

Dated, New York, N. Y., April 4, 1936.

C. M. Bracelen, Chas. T. Russell, Edward L. Blackman, Alan J. McBean, Solicitors for Plaintiffs and Intervening Plaintiffs, Office and Post Office Address, No. 195 Broadway, New York City, New York. Allen T. Klots, Hayden N. Smith, Solicitors for Additional Plaintiffs, Office and Post Office Address, No. 32 Liberty Street, New York City, New York.

[fol. 827] IN UNITED STATES DISTRICT COURT

[Title omitted]

AFFIDAVIT OF SERVICE—Filed April 6, 1936

STATE OF NEW YORK,
County of New York, ss:

S. Whitney Landon, being first duly sworn, deposes and says:

That he is an attorney and counselor-at-law in the offices of the American Telephone and Telegraph Company, one of the plaintiffs herein, and that on the 4th day of April, 1936, at about 5:40 o'clock P. M., he served the annexed Notice of Appeal upon the Honorable John C. Bennett, General Attorney of the State of New York, by depositing on said date and at said time in the City Hall Post Office, [fol. 828] Broadway and Park Row, Borough of Manhattan, City and State of New York, a true copy of said Notice, securely enclosed in a sealed wrapper bearing first class postage and addressed as follows:

The Honorable John C. Bennett, Attorney General of the State of New York, Albany, New York.

S. Whitney Landon.

Sworn to before me this 4th day of April, 1936. Charles M. Deal, Notary Public, Kings Co., No. 363. Reg. No. 7148, Cert. Filed in N. Y. Co. No. 393, Reg. No. 7-D-225. Commission Expires March 30, 1937. (Seal.)

[fols. 829-836] Citation, in usual form, showing service on Harold F. Collins et al., filed April 6, 1936, omitted in printing.

[fol. 837] IN UNITED STATES DISTRICT COURT

[Title omitted]

ORDER EXTENDING TIME—Filed May 1, 1936

For good cause shown, it is hereby ordered that the time within which to file the transcript of record on appeal and to docket the appeal of the plaintiffs, additional plaintiffs and intervening plaintiffs, in the above entitled cause, in the Supreme Court of the United States, be and the same is hereby extended to and including June 3, 1936, and that the time for approval and filing of the statement of evidence (pursuant to Equity Rule No. 75) to be included in [fol. 838] said transcript of record, be likewise extended.

Dated April 30, 1936.

Jno. C. Knox, United States District Judge.

All parties consent to the entry by the United States District Court of the above order.

Dated April 29, 1936.

Stanley Reed, Solicitor General for United States of America. Frank Roberson, for Federal Communications Commission. John E. Benton, for National Association of Railroad and Utilities Commissioners. Alan J. McBean, for Plaintiffs and Intervening Plaintiffs. Allen T. Klots, for Additional Plaintiffs.

[fol. 839] IN UNITED STATES DISTRICT COURT

[Title omitted]

STIPULATION IN LIEU OF PRÆCIPE—Filed May 14, 1936

To the Clerk of the United States District Court for the Southern District of New York:

It is hereby stipulated and agreed by and between the parties hereto, by their respective counsel, that the transcript of record for appeal in the above entitled cause to the Supreme Court of the United States shall consist of

the following portions of the record in this case, the same as if directed by præcipe for record, and you are requested to incorporate in such transcript, certified as required by law, the following:

[fol. 840] 1. Plaintiffs' Bill of Complaint and Exhibit A and Exhibit B thereto attached.

2. Notice of Appearance of Additional Plaintiffs.

3. Additional Plaintiffs' Bill of Complaint.

4. Order approving Additional Plaintiffs' appearance and order to show cause issued on Additional Plaintiffs' motion.

5. Order to show cause issued on Plaintiffs' motion.

6. Response of Federal Communications Commission to order to show cause omitting affidavits.

7. Notice of and petition for leave to intervene of Intervening Plaintiffs omitting proposed pleading.

8. Order allowing intervention of Intervening Plaintiffs.

9. Bill of Intervention of Intervening Plaintiffs and Exhibit A thereto annexed.

10. Answer of Federal Communications Commission to Plaintiffs' Bill of Complaint.

11. Petition for leave to intervene of National Association of Railroad and Utilities Commissioners.

12. Order allowing intervention of National Association of Railroad and Utilities Commissioners.

[fol. 841] 13. Answer of National Association of Railroad and Utilities Commissioners.

14. Answer of Federal Communications Commission to Additional Plaintiffs' Bill of Complaint.

15. Answer of Federal Communications Commission to Intervening Plaintiffs' Bill of Intervention.

16. Answer of United States of America to Plaintiffs' Bill of Complaint.

17. Answer of United States of America to Additional Plaintiffs' Bill of Complaint.

18. Answer of United States of America to Intervening Plaintiffs' Bill of Intervention.

19. Statement of Evidence.

20. Stipulation as to Statement of Evidence and Waiver of Lodgment and Notice of Filing.

21. Order Approving Statement of Evidence.

22. Order granting temporary stay.

23. Opinion of District Court.

24. Findings of Fact and Conclusions of Law of District Court.
25. Additional Findings of Fact of District Court.
26. Final Decree.
27. Petition for Appeal.
[fol. 842] 28. Assignments of Error.
29. Statement Showing basis of Jurisdiction of Supreme Court.
30. Order allowing Appeal.
31. Approved Appeal Bond.
32. Notice to Attorney General of the State of New York together with proof of service.
33. Citation on appeal together with proof of service.
34. Notice to Appellees, pursuant to Rule 12, Paragraph 2, together with proof of service.
35. Order extending time to file transcript and docket appeal.
36. This stipulation for transcript of record.

Dated May 12, 1936.

C. M. Bracelen, Chas. T. Russell, Edward L. Blackman, Alan J. McBean, Solicitors for Plaintiffs and Intervening Plaintiffs. Allen T. Klots, Hayden N. Smith, Solicitors for Additional Plaintiffs. [fol. 843] Harold F. Collins, Special Assistant to the Attorney General, Solicitor for Defendant, United States of America. Hampson Gary, Frank Roberson, W. D. Humphrey, Solicitors for Defendant, Federal Communications Commission. John E. Benton, Solicitor for Intervening Defendant, National Association of Railroad and Utilities Commissioners.

So Ordered Jno. C. Knox, U. S. D. J.

[File endorsement omitted.]

[fol. 844] IN UNITED STATES DISTRICT COURT

[Title omitted]

STIPULATION AS TO CORRECTNESS OF TRANSCRIPT OF RECORD

It is hereby stipulated and agreed by and between the parties hereto by their respective counsel that the foregoing is a true transcript of the record of the said District Court in the above entitled cause as agreed on by the parties.

Dated: May 12, 1936.

C. M. Bracelen, Chas. T. Russell, Edward L. Blackman, Alan J. McBean, Solicitors for Plaintiffs and [fol. 845] Intervening Plaintiffs. Allen T. Klots, Hayden N. Smith, Solicitors for Additional Plaintiffs. Harold F. Collins, Special Assistant to the Attorney General, Solicitor for Defendant, United States of America. Hampson Gary, Frank Roberson, W. D. Humphrey, Solicitors for Defendant, Federal Communications Commission. John E. Benton, Solicitor for Intervening Defendant, National Association of Railroad and Utilities Commissioners.

[fols. 846 & 847] Clerk's certificate to foregoing transcript omitted in printing.

[fol. 848] SUPREME COURT OF THE UNITED STATES

STATEMENT OF POINTS UPON WHICH APPELLANTS INTEND TO RELY AND DESIGNATION OF PARTS OF RECORD NECESSARY FOR CONSIDERATION THEREOF—Filed May 22, 1936

Pursuant to the provisions of Supreme Court Rule 13, Paragraph 9, appellants state that the points upon which they intend to rely upon their appeal herein are as follows:

[fol. 849] I

The "original cost" provisions of the order of the Federal Communications Commission here in issue, which require property investment accounts to be kept on the basis of cost to the public utility which first dedicated the prop-

erty to public use, are void because they are so arbitrary and unreasonable as to be beyond the authority of the Commission to prescribe and deprive the appellants of their property, including the right to keep a reasonable set of accounts, in violation of the due process clause of the Fifth Amendment to the Constitution of the United States, in that:

a. They require appellants to keep their property investment accounts so as to misrepresent their investment in property.

b. They prevent appellants from charging any depreciation expense on a part of their actual investment in depreciable property.

c. In effect, they require a retroactive change in the accounts of transactions entered into with governmental approval, the records of which have been correctly kept in accordance with rules prescribed by law.

[fol. 850] d. They are unreasonably burdensome and expensive, and serve no useful purpose except the recording of information which, when needed, could be made available, in supplementary statements, pursuant to Section 213 (c) of the Communications Act of 1934, at relatively minor expense and without causing the accounts to misrepresent the facts.

The District Court erred in holding these provisions valid against these objections of appellants. (Assignments of Error 1 to 6 and 23 to 30, inclusive.)

II

The provision of said order that the difference between cost to the accounting company and cost to the former owner which first devoted the property to the public use shall be disposed of, written off or amortized, not in accordance with any rule, classification or standard contained in said accounting system or elsewhere, but as the Commission may direct in the case of each individual property acquisition, is void. The Commission's authority is limited to the making of rules, regulations and classifications in accordance with which all telephone companies, or all with-

in a class, shall keep their accounts, and it has no authority to order the making of such specific accounting entry as it may direct with respect to a transaction as to which it has [fol. 851] made no accounting rules, regulations or classifications. The District Court erred in holding said provision valid against this objection of appellants. (Assignments of Error 7, 8, 9 and 31.)

III

Instruction 2 (B.1) of said order provides:

"All charges to the accounts prescribed in this classification for telephone plant, income, operating revenues, and operating expenses shall be just and reasonable and any payments by the company in excess of such just and reasonable charges shall be included in account 323, 'Miscellaneous income charges.'"

This requirement is so arbitrary and unreasonable as to be beyond the authority of the Commission to prescribe and deprives appellants of their rights under the due process clause of the Fifth Amendment to the Constitution of the United States, in that:

a. It is contrary to the fundamental principles of correct accounting and would compel a falsification of appellants' accounts.

b. It lays down a rule of accounting, to which appellants must conform on pain of the statutory penalties, so vague and indefinite as not to constitute a legal standard of conduct.

The District Court erred in holding said instruction valid against these objections of appellants. (Assignments of Error 10 to 14, inclusive, and 34.)

[fol. 852] IV

Said order requires appellants to divide a substantial part of their investment among three accounts (Accounts 100.1, 100.3 and 103), depending on whether the plant involved is used or held for imminent use or held for use which is not imminent. The instructions of said order with respect to what property shall be entered in each of these accounts lay down rules of accounting, to which appellants must conform on pain of the statutory penalties,

so vague and indefinite as not to constitute a legal standard of conduct, and are therefore arbitrary and deprive appellants of their rights under the due process clause of the Fifth Amendment to the Constitution of the United States. The District Court erred in holding these instructions valid against this objection of the appellants. (Assignments of Error 15 to 19, inclusive, 32 and 33.)

V

The provisions challenged in Points I and IV, above, are non-severable from the other provisions of said order, and the order as a whole is therefore void because of the illegality of said provisions. The District Court erred in holding such provisions to be severable. (Assignments of Error 20 to 22, inclusive, and 35.)

[fol. 853] Appellants further state that they think that the whole of the record, as filed, with the exceptions hereinafter stated, is necessary for the consideration of the foregoing points, and that the same is necessary to be printed for the consideration of the court upon the present appeal. The parts not so necessary to be printed are:

1. Commencing with the phrase "As a consequence" in line 3, page 376, to and including the word "accounting" in line 3, page 379.

2. Commencing with the heading "II.", page 380, to and including the word "methods." in line 16, page 381.

3. Commencing with the heading "II.", page 396, to and including the word "accounting" in the last line on page 397.

4. Commencing with the heading "IV.", page 400, to and including the word "use" in the last line on page 405.

5. Commencing with the item "3." in line 13, page 410, to and including "6)." in line 17.

6. Commencing with the heading "3.", page 418, to and including the word "property," the last word in line 25 on page 421.

7. Commencing with the word "Among" in line 7, page 427, to and including the word "stated" in line 18.

8. Commencing with the words "Said system" in line 20, page 443, to and including the word "benefit." in line 13 on page 445.

9. Commencing with the words "Said system" in line 7, page 448, to and including the word "attached.)" in line 20 on page 449.

[fol. 854] 10. Commencing with the words "Telephone Division" in line 15, page 452, to and including the figure "$800,000." in line 18 on page 453.

11. Page 455 to page 460 inclusive.

12. Commencing with the figure "8" in line 18, page 582, to and including the word "accounts." in line 13 on page 583.

13. Commencing with the heading "II", page 606, to and including the word "information" in line 21 on page 608.

14. Commencing with the heading "VIII.", page 612, to and including the word "recorded." in line 7 on page 613.

15. Commencing with the heading "X.", page 613, to and including the word "available." in line 19 on page 614.

16. Commencing with the heading "Allegation 8.", page 622, to and including the word "discontinued." in line 18.

17. Commencing with the heading "Allegation 10.", page 623, to and including the word "applicable." in line 20.

18. Commencing with the heading "Allegation 14.", page 624, to and including the word "companies." in the last line on page 625.

19. Commencing with the item "5." in line 28, page 640, to and including the word "acquired." in line 2 on page 641.

20. Commencing with the item "7." in line 9, page 641, to and including the word "Use." " in line 13.

21. Commencing with the heading "5.", page 651, to and including the word "investments." in line 5 on page 653.

[fol. 855] 22. Commencing with the heading "7.", page 653, to and including the word "Commission." in line 21 on page 654.

23. Commencing with the heading "22." in line 6, page 666, to and including the word "necessary." in line 20 on page 669.

24. Commencing with the words "except that additional complaints" in line 11, page 670, to and including the word "performed." in the last line on page 673.

25. Commencing with the heading "3.", page 680, to and including the word "decision." " in line 30.

26. Commencing with the heading "6.", page 682, to and including the word "cases." in line 13 on page 683.

27. Commencing with the heading "8.", page 684, to and including the word "accounts." in line 14 on page 685.

28. Commencing with the heading "2.", page 695, to and including the word "surplus." in line 3 on page 697.

29. Commencing with the heading "5.", page 698, to and including the word "necessary." in line 2 on page 699.

30. Commencing with the heading "9.", page 704, to and including the word "rates." in line 13 on page 705.

31. Commencing with the heading "6.", page 715, to and including the word "only." in line 8 on page 716.

32. Commencing with the words "It is my opinion that the position" in line 24, page 716, to and including the word "condition." in line 19 on page 717.

[fol. 856] 33. Page 728 to page 730 inclusive.

34. Commencing with the heading "II", page 734, to and including the word "diligence." in line 2 on page 735.

Dated May 21, 1936.

C. M. Bracelen, Chas. T. Russell, Edward L. Blackman, Alan J. McBean, Solicitors for Appellants, American Telephone and Telegraph Company et al. and Eastern Telephone and Telegraph Company et al. Allen T. Klots, Solicitor for Appellants, Ohio Associated Telephone Company et al.

Due and timely service of the above and foregoing statement is hereby acknowledged this 22nd day of May, 1936.

Harold F. Collins, Special Assistant to the Attorney General, Solicitor for Appellee, United States of [fol. 857] America. Hampson Gary, Frank Roberson, W. D. Humphrey, Solicitors for Appellee, Federal Communications Commission. John E. Burton, Clyde S. Bailey, Solicitors for Appellee, National Association of Railroad and Utilities Commissioners.

[fol. 858] [File endorsement omitted.]

Endorsed on cover: File No. 40,608. S. New York, D. C. U. S. Term No. 74. American Telephone and Telegraph Company et al., appellants, vs. The United States of America, Federal Communications Commission, and National Association of Railroad and Utilities Commissioners. Filed May 22, 1936. Term No. 74, O. T., 1936.

FILE COPY

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1939

No. [redacted] 74

AMERICAN TELEPHONE AND TELEGRAPH COMPANY ET AL.,

Appellants,

vs.

THE UNITED STATES OF AMERICA, FEDERAL COMMUNICATIONS COMMISSION, AND NATIONAL ASSOCIATION OF RAILROAD AND UTILITIES COMMISSIONERS.

APPEAL FROM THE DISTRICT COURT OF THE UNITED STATES FOR THE SOUTHERN DISTRICT OF NEW YORK.

STATEMENT AS TO JURISDICTION.

C. M. Bracken,
Orie T. Russell,
Edward L. Bracken,
Allan C. McBean,
Albert J. Kelly,
Harold K. Sutton,
Counsel for Appellants.

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IN THE

DISTRICT COURT OF THE UNITED STATES FOR THE SOUTHERN DISTRICT OF NEW YORK

In Equity.

No. 81-366

AMERICAN TELEPHONE AND TELEGRAPH COMPANY ET AL.,

Plaintiffs;

OHIO ASSOCIATED TELEPHONE COMPANY ET AL.,

Additional Plaintiffs;

EASTERN TELEPHONE AND TELEGRAPH COMPANY ET AL.,

Intervening Plaintiffs,

vs.

UNITED STATES OF AMERICA AND FEDERAL COMMUNICATIONS COMMISSION,

Defendants,

NATIONAL ASSOCIATION OF RAILROAD AND UTILITES COMMISSIONERS,

Intervening Defendant.

STATEMENT OF JURISDICTION.

Filed April 6, 1936.

Pursuant to Rule 12 of the Supreme Court of the United States, plaintiffs, intervening plaintiffs and additional plaintiffs (hereinafter referred to as plaintiffs), in support

of their petition for appeal, file this their statement of the basis upon which it is contended that the Supreme Court of the United States has jurisdiction upon appeal to review the final decree of this court in the above entitled cause:

(a)

Statutory Provisions Sustaining Jurisdiction.

The statutory provisions which sustain such jurisdiction of the Supreme Court of the United States are as follows:

1. Section 402 (a) of the Communications Act of 1934 (48 Stat. L. 1064, 1093; U. S. C., Title 47, Section 402 (a)), which reads as follows:

> "SEC. 402. (a) The provisions of the Act of October 22, 1913 (38 Stat. 219), relating to the enforcing or setting aside of the orders of the Interstate Commerce Commission, are hereby made applicable to suits to enforce, enjoin, set aside, annul, or suspend any order of the Commission under this Act (except any order of the Commission granting or refusing an application for a construction permit for a radio station, or for a radio station license, or for renewal of an existing radio station license, or for modification of an existing radio station license), and such suits are hereby authorized to be brought as provided in that act."

2. Act of October 22, 1913—Urgent Deficiencies Appropriations Act (38 Stat. L. 219, 220; U. S. C., Title 28, Sections 47 and 47a). This act authorizes direct appeals to the Supreme Court of the United States from decrees of this Court granting or denying an injunction against the operation of orders of the Interstate Commerce Commission such as the order involved in this cause.

(b)

Order of the Federal Communications Commission, the Validity of Which is Involved.

This appeal involves the validity of that certain order of the Federal Communications Commission designated "Telephone Division Order No. 7-C," which order prescribes a Uniform System of Accounts for telephone companies subject to the provisions of the Communications Act of 1934 and having average annual operating revenues exceeding $50,000, and requires all such telephone companies to keep all accounts in conformity therewith after December 31, 1935.

The said order and the instructions constituting the system of accounts prescribed thereby comprise, as officially published by the said Federal Communications Commission, 121 printed pages, and it is impracticable to set them forth herein verbatim or to further summarize their pertinent provisions. A copy of said order and instructions is attached to the bill of complaint herein as Exhibit B.

Said order of the Federal Communications Commission was issued pursuant to the authorization contained in Section 220 of said Communications Act of 1934, sub-sections (a) and (g) thereof being as follows:

> "SEC. 220. (a) The Commission may, in its discretion, prescribe the forms of any and all accounts, records, and memoranda to be kept by carriers subject to this Act, including the accounts, records, and memoranda of the movement of traffic, as well as of the receipts and expenditures of moneys.
>
> • • • • • • •
>
> "(g) After the Commission has prescribed the forms and manner of keeping of accounts, records, and memoranda to be kept by any person as herein pro-

vided, it shall be unlawful for such person to keep any other accounts, records, or memoranda than those so prescribed or such as may be approved by the Commission or to keep the accounts in any other manner than that prescribed or approved by the Commission. Notice of alterations by the Commission in the required manner or form of keeping accounts shall be given to such persons by the Commission at least six months before the same are to take effect."

(c)

Dates of Decree and of Application for Appeal.

The decree of this court sought to be reviewed was entered March 24th, 1936.

The application for appeal was presented on April 4th, 1936.

(d)

Nature of Case.

The suit was brought in the District Court of the United States for the Southern District of New York and was heard by a specially constituted court of three judges, pursuant to the provisions of said Urgent Deficiencies Appropriations Act of October 22, 1913. The purpose thereof was to enjoin, set aside and annul the said order of the Federal Communications Commission designated "Telephone Division Order No. 7-C", which requires plaintiffs, on and after January 1, 1936, to keep all their accounts in accordance with the system of accounts prescribed thereby. The bills of complaint allege that numerous requirements of said system are so contrary to the fundamental principles of correct accounting and so arbitrary and unreasonable as to amount to an abuse of the Commission's power, are beyond the authority of the Commission and are void, and that they will cause plaintiffs serious financial loss

and will deprive them of their right to keep a reasonable and adequate set of accounts, in violation of the due process clause of the Fifth Amendment to the Constitution of the United States; that certain requirements of said system lay down rules which are so vague as not to constitute legal standards of conduct, and that the enforcement thereof by the penalties prescribed by the said Act or otherwise would violate the rights of plaintiffs to due process of law as guaranteed by the Fifth Amendment to the Constitution of the United States. Plaintiffs alleged that the requirements complained of were nonseverable from the other provisions of said system, and prayed that said order and system of accounts as a whole be enjoined. The final decree of the court, from which this appeal is sought, denied the prayer of the plaintiffs that said order and system of accounts as a whole be permanently enjoined, and said decree enjoined the enforcement of only two of the several requirements complained of. The decree therefore constitutes a decision adverse to plaintiffs.

There is appended hereto a copy of the opinion delivered by this court upon the rendering of the decree sought to be reviewed.

(e)

Cases Sustaining Jurisdiction.

Since the enactment of the Communications Act of 1934, no cases involving the validity of an order of the Federal Communications Commission have been taken on appeal to the Supreme Court of the United States. There are, therefore, no cases reported in which Section 402 (a) of the Communications Act of 1934 has been interpreted or commented upon. However, Section 402 (a) merely provides that the provisions of the Urgent Deficiencies Appropriations Act of October 22, 1913, relating to the enforcement or setting aside or orders of the Interstate Com-

merce Commission are made applicable to suits to enforce, enjoin, set aside, annul or suspend orders of the Federal Communications Commission.

The following cases, involving orders of the Interstate Commerce Commission and brought pursuant to the provisions of said Urgent Deficiencies Appropriations Act, are cited as sustaining the jurisdiction of the Supreme Court of the United States upon direct appeal to review the decree herein:

Louisville and Nashville R. Co. v. *U. S.*, 238 U. S. 1, 10;
Colorado v. *United States, et al.*, 271 U. S. 153, 161;
Home Furniture Co. et al. v. *United States, et al.*, 271 U. S. 456, 459;
St. Louis and O'Fallon R. Co. v. *United States*, 279 U. S. 461, 481-482;
Norfolk & Western Ry. Co. v. *United States*, 287 U. S. 134.

It, is, therefore, respectfully submitted that the Supreme Court of the United States has jurisdiction of this appeal by virtue of Section 402 (a) of the Communications Act of 1934 (U. S. C., Title 47, Section 402 (a)), and the Urgent Deficiencies Appropriations Act of October 22, 1913 (U. S. C., Title 28, Sections 47 and 47 (a)).

Dated April 4th, 1936.

C. M. Bracelen,
Chas. T. Russell,
Edward L. Blackman,
Alan J. McBean,
Solicitors for Plaintiffs and Intervening Plaintiffs;
Allen T. Klots,
Hayden N. Smith,
Solicitors for Additional Plaintiffs.

APPENDIX.

IN THE DISTRICT COURT OF THE UNITED STATES FOR THE SOUTHERN DISTRICT OF NEW YORK.

AMERICAN TELEPHONE AND TELEGRAPH COMPANY *et al.*, *Plaintiffs;* OHIO ASSOCIATED TELEPHONE COMPANY *et al.*, *Additional Plaintiffs;* EASTERN TELEPHONE AND TELEGRAPH COMPANY *et al.*, *Intervening Plaintiffs,*

vs.

UNITED STATES OF AMERICA AND FEDERAL COMMUNICATIONS COMMISSION, *Defendants;* NATIONAL ASSOCIATION OF RAILROAD AND UTILITIES COMMISSIONERS, *Intervening Defendant.*

Opinion.

Before MARTIN T. MANTON and AUGUSTUS N. HAND, Circuit Judges, and JOHN C. KNOX, District Judge, Constituting a Statutory Court under 28 U. S. C. 47.

MANTON, Circuit Judge:

Plaintiffs, common carriers of communication by wire, file this bill under the Urgent Deficiencies Act, October 22, 1913, c. 32, 38 Stat. 208, 219, made applicable by §402(a) of the Communications Act [June 19, 1934, c. 652, §402(a), 47 U. S. C. 402(a), 48 Stat. 1093]. They seek to restrain the Federal Communications Commission from enforcing its Order No. 7-C issued June 19, 1935 and effective January 1, 1936 to govern the system of accounts for telephone companies engaged in interstate commerce and having average annual operating revenues exceeding $50,000. A temporary stay was granted pendi[illegible] decision on the permanent injunction. The issues are submitted for final determination on affidavits and the arguments thereon.

The accounting system now in operation was promulgated by the Interstate Commerce Commission as the "Uniform System of Accounts for Telephone Companies, First Revised Issue," effective from January 1, 1933. Upon ob-

jections by twenty-two state commissions, the Interstate Commerce Commission had taken under advisement suggested changes in this 1933 system. Its inquiry ended very shortly before jurisdiction over telephone companies was transferred to the Federal Communications Commission created by the Communications Act of June 19, 1934. In view of this fact, the Interstate Commerce Commission, although it issued no order, rendered a report of the proceedings before it, for the convenience of the incoming Commission [Accounting Rules for Telephone Companies, 203 I. C. C. 13]. In this report, some of the matters now objected to, were discussed and disapproved. The Communications Commission, after supplemental investigation, hearings and conferences, did not follow the Interstate Commerce Commission in its disapproval of these provisions and incorporated them in the system now under review. The National Association of Railroad and Public Utility Commissioners, which claims to represent the commissions having jurisdiction over telephone companies in forty-six states, has endorsed the proposed system and has appeared in this case by intervening as a party defendant. In addition, the New York State Public Service Commission pleads for the order as *amicus curiæ*.

The attack on the order requiring the uniform system of accounts is based upon the claim that it is invalid because it violates the Fifth Amendment to the Constitution and §404 of the Communications Act, (a) since it is unsupported by a report stating conclusions and basic findings; (b) the requirements exceed the statutory power of the Commission and are so contrary to the fundamental principles of correct accounting as to constitute an abuse of that power in so far as they treat of original cost, contributions, certain classifications of telephone plant and depreciation thereon, and just and reasonable charges; (c) amendments in requiring obedience to standards so vague and indefinite as to be unintelligible, or violate the Fifth and Sixth Amendments.

Before other discussion, it should be settled that the order is not void for lack of a report stating the conclusions and findings of fact by the Commission. Section 220(a) of the Communications Act provides:

> "The Commission may, in its discretion, prescribe the forms of any and all accounts, records, and memoranda to be kept by carriers subject to this chapter * * *."

There is an identical provision in the Interstate Commerce Act, §20(5). When a system of accounts is laid down under these sections, the action is a legislative, rather than a judicial function. It is making a new rule to be applied in the future, not applying an already existent rule to past facts. This is the characteristic of legislation. See *Keller* v. *Potomac Electric Power Co.*, 261 U. S. 428, 440; *Prentis* v. *Atlantic Coast Line Co.*, 211 U. S. 210, 226. And to claim that findings are essential to support this order is to ignore this difference. Assigned Car Cases, 274 U. S. 564, 583. An administrative body can exercise a delegated legislative function without first reporting the data upon which it decided that the proposed rule should be established. *Pacific States Box & Basket Co.* v. *White*, 80 L. Ed. 133. Since the Commission is authorized to act "in its discretion", there is no requirement that it find the facts upon which its authority to act is conditioned as in *Atchison, Topeka & Santa Fe Ry. Co.* v. *United States*, 295 U. S. 193; *United States* v. *Chicago, Milwaukee, St. Paul & Pac. R. Co.*, 294 U. S. 499; *United States* v. *Baltimore & Ohio R. R. Co.*, 293 U. S. 454. The case last cited points out the difference at p. 462. In holding an order void for lack of a finding on a jurisdictional fact, the court said:

> "The Act (Boiler Inspection Act) does not confer upon the Commission legislative authority to require the adoption on locomotives of such services as, *in its discretion*, it may from time to time deem desirable."

Section 220 (a) conferring power to prescribe the accounting system does confer upon the Commission power to act in its discretion.

Nor does § 404 of the Act render an order under § 220 (a) void if a report is lacking. Section 404 provides:

> "Whenever an investigation shall be made by the Commission it shall be its duty to make a report in

writing in respect thereto, which shall state the conclusions of the Commission, together with its decision, order or requirement in the premises; and in case damages are awarded such report shall include the findings of fact on which the award is made."

This section requires findings of fact only in the event damages are awarded. The order No. 7-C does not award damages. Although the Commission, as outlined above, did extensive preliminary work before entering the order, a report of its conclusions is not a condition to the order's validity. The conclusions of the Commission are very evident from the order itself.

In support of this position, there is the fact that § 404 and 220(a) of the Communications Act are identical with § 14(1) and § 20(5) of the Interstate Commerce Act. It has not been the practice of the Interstate Commerce Commission to preface its general accounting orders with reports, and the incorporation of these sections in the Communications Act is an indication that Congress approved this administrative interpretation. See *McGaughen* v. *Hershey Chocolate Co.*, 283 U. S. 488, 492, 3; *National Lead Co.* v. *United States*, 252 U. S. 140, 146.

The Communications Act made the judicial procedure applicable in proceedings to enforce or test the validity of the Communications Commission orders similar to like proceedings affecting the orders of the Interstate Commerce Commission (§ 402 [a]). We must, therefore, in reviewing this order, be guided by the rule that in respect to orders of the Commission, the court may not "under the guise of exerting judicial power, usurp merely administrative functions by setting aside a lawful administrative order upon our conception as to whether the administrative power has been wisely exercised." *Interstate Commerce Comm.* v. *Illinois Central R. R. Co.*, 215 U. S. 452, 470. See *Interstate Commerce Comm.* v. *Union Pacific R. R. Co.*, 222 U. S. 541, 547. It is not enough to reason that the order is unwise, inexpedient or at variance with the court's own views as to what is practicable. This rule guides judicial review of any legis-

lative act. *Chicago, Burlington & Quincy R. R. Co.* v. *McGuire,* 219 U. S. 549, 569.

We have already pointed out that the order prescribing a uniform system of accounts is of a legislative character. When § 20(5) of the Interstate Commerce Act was before the Supreme Court in *Interstate Commerce Commission* v. *Goodrich Transit Co.* (224 U. S. 194), and *Kansas City Southern Railway Co.* v. *United States* (231 U. S. 423), the court, while characterizing the Commission's power as legislative, also held it not unlawfully delegated saying at 214:

> "The Congress may not delegate its purely legislative power to a commission, but, having laid down the general rules of action under which a commission shall proceed, it may require of that commission the application of such rules to particular situations and the investigation of facts, with a view to making orders in a particular matter within the rules laid by the Congress * * *."

And referring to § 20, said:

> "* * * The Commission is permitted, in its discretion, to require a uniform system of accounting, and to prohibit other methods of accounting than those which the Commission may prescribe. In other words, Congress had laid down general rules for the guidance of the Commission, leaving to it merely the carrying out of details in the exercise of the powers so conferred. This, we think, is not a delegation of legislative authority."

No commission accounting order is to be reviewed judicially for the purpose of determining whether it conforms to the court's views as to what constitutes proper, efficient, practical accounting methods but it is for the court to say only whether the commission has acted within statutory and constitutional limits. See *Norfolk & Western R. R. Co.* v. *United States,* 287 U. S. 134, 143.

Therefore, our inquiry as far as it goes beyond a consideration of power within the statute is merely whether the order is "so entirely at odds with fundamental principles

of correct accounting as to manifest an abuse of power." See *Chesapeake & Ohio Ry. Co.* v. *United States*, 5 Fed. Supp. 7, 14 (E. D. N. Y.).

Section 213(c) in specific terms authorized the commission to obtain from telephone carriers at any time information concerning original cost of their properties which may be needed for rate fixing purposes. And it is asserted by plaintiffs, that this section is the full measure of the Commission's authority to require information as to original cost and that an order under § 220(a) requiring data in respect of original cost to be kept in a system of accounting may not be prescribed. Section 220(a) authorized the Commission in its discretion to "prescribe the forms of any and all accounts, records and memorandum to be kept by the carrier". The powers conferred by § 213(c) are not restrictive of § 220(a) nor does the latter section restrict the former. The two sections are capable of complementary treatment.

The requirement that original cost be set forth in accounting records of the telephone companies serves to complete the picture of value in revealing the property's financial background and showing the relationship of a carrier's monetary return to the original as well as to its own investment. It aids the Commission in its duty to determine from all the pertinent circumstances and factors, the just and reasonable rates which the carrier may exact from its service. Original cost is a relevant factor. *Smyth* v. *Ames*, 169 U. S. 466, 547; *Los Angeles Co.* v. *R. R. Comm.*, 289 U. S. 287, 306, cf. § 213(a) of the Act. The object of the system of accounts might well be to display the pertinent financial operation and throw light upon its present condition. *Kansas City Southern Ry.* v. *U. S., supra,* at p. 440. Original cost as a segregated item on a balance sheet may serve to reveal actualities which may be pertinent in fixing a rate base on the capitalized earning power of a property purchased. In making readily available facts which would tend to expose discrepancies in valuation, it cannot be said the system is so arbitrary as to be beyond the commission's power. Forty-seven State public utility bodies acquiesce

in the proposed requirements. This is not evidence of unreasonableness.

The new system requires that when telephone plant in service is acquired, the amount paid therefor shall be charged to account 276 (Telephone plant required). The original cost of the property, estimated if not known, shall then be charged (debited) to the appropriate telephone plant account, whether "in service" (100.1), "under construction" (100.2), or "held for future use" (100.3) and credited to account 276. After debits to 276 for "contributions", and for reserve requirements for depreciation and amortization to date of the plant acquired, the amount remaining in 276 shall be debited or credited as appropriated to account 100.4 (Telephone plant acquisition adjustment). As to 100.4, the system provides: "The amounts recorded in this account with respect to each property acquisition shall be disposed of, written off, or provision shall be made for the amortization thereof in such manner as this Commission may direct [100.4(c)]." "Original cost" as used is defined as "the actual money cost of or the current money value of any consideration other than money exchanged for property at the time when it was first dedicated to the public use, whether by the accounting company or by a predecessor public utility" (instruction 3-S-1).

The plaintiffs direct at this requirement the objection that these provisions violate the fundamental principles of accounting in the following respects: although 100.1, 100.2, 100.3 and 100.4 if added together immediately will show the company's actual investment in its plant, since 100.4 must be written off at the will of the Commission, it will be necessary to carry a surplus reserve against this possible write-off. Once the write-off has been made, they declare that no combination of balances will reflect the company's actual investment. And they object further, because there can be no depreciation charge to any amount in account 100.4.

In considering the merits of these objections, it becomes necessary to examine, for purposes of comparison, the system now in effect which the plaintiffs do not attack as unreasonable and which they seek to retain. Under the present system, account 278 "undistributed cost of prop-

erty'' performs a function similar to account 100.4. Under it, when a purchase is made, the estimated current value of the land, the current cost new (estimated if not known) of certain other telephone plant, the original cost of franchises, and the cost of uncompleted projects are charged to their corresponding accounts. After crediting to reserve accounts, the estimated depreciation and amortization applicable, the difference between the total of the foregoing amounts and the cost to the accounting company of the plant acquired is debited or credited to 278, ''undistributed cost of property.'' Account 278 is classed as a ''telephone plant account'' and is reported in the balance sheet as part of account 100 (Telephone plant).

As an alternative, the Commission may permit the transfer of the amounts in the ''telephone plant accounts'' and in ''depreciation and amortization reserve accounts'' as carried in the books of the vendor company to the books of the purchaser. In some instances, the amounts actually paid by the purchasing companies have been recorded in the ''plant'' accounts. Thus, actual cost, current cost new at the time of purchase, and original cost at the time of first dedication are in use at present as the bases of various telephone plant accounts. The amount in 278 of the present system is subject to no depreciation and may be written off only through surplus.

On a comparison of the two systems, that of this Commission seems to more accurately reflect the condition and record the history of the plant. Account 100.4 is listed among investments. It can be subdivided so that there can be segregated any amount therein not representing (1) the cost of elimination of competition; (2) payment to an affiliate at a price in excess of cost to it with a profit returnable to the purchasing company in the form of dividends or otherwise; and (3) any other element not expended in public interest.

This segregated amount would receive the same treatment substantially in the rate and depreciation basis as would amounts appearing in 100.1 ''Telephone plant in service''. In this light, it appears that the proposed system merely provides segregation, and that the addition of

the amounts in these investment accounts 100.1 through 100.4 would accurately picture the legitimate investments of the purchasing company.

To follow the plaintiffs in their argument that a reserve of surplus must be maintained against 100.4 and that this is fundamentally wrong, would be to ignore the similarity between 278 of the present system and 100.4 of the proposed system, and further it requires the assumption that the Commission will act improperly in the future under 100.4(c). This cannot be presumed. The order provides for alternatives adaptable to the facts of individual cases. This flexibility distinguishes the system at bar from that held invalid in *New York Edison Co.* v. *Maltbie* (344 A. D. [N. Y.] 685). This cannot be held, before any order under 100.4(c) has been made by the Commission, to be such an arbitrary method of accounting that the order imposing it is void.

The same argument applies to the objection that no depreciation is allowed against item 100.4 "acquisition adjustments". This complaint anticipates arbitrary action by the Commission, under 100.4(c) which authorizes handling of this item through amortization. The effect would be the same as writing down through depreciation, and until the Commission acts so that the accounts become so contrary to the principles of correct accounting as to constitute the Commission's order arbitrary and unreasonable, the Commission is within its powers. The court need not agree the accounting proposed is the best method, but at this stage it cannot be said the provision is arbitrary. The objection is made that the Commission's refusal to act properly within 100.4(c) would constitute a negative order, non-reviewable within the doctrine of *Proctor & Gamble* v. *United States*, 225 U. S. 282. This would not cut off the plaintiffs' right of attacking the system as it would apply to them after such a refusal. The appeal need not be on the order denying relief but can be against the system as its operation is affected by such denial.

There is no deprivation of property involved here. The Supreme Court has noted that the question merely concerned accounting and that there was no occasion to hold

the order invalid as a deprivation of property until actual damage was threatened by it as in the use of an improper rate base in setting rates. *Norfolk & Western Ry. Co.* v. *United States*, 287 U. S. 134; *United States* v. *Los Angeles & Salt Lake R. R. Co.*, 273 U. S. 299.

The plaintiffs object that no depreciation is allowed on property held for future use in account 100.3. Except in those rare instances when the entire cost of depreciation covers only the wear and tear on equipment in use, the plant held in reserve will depreciate because of obsolescence or deterioration as it is not entirely dependent on use. The exclusion of depreciation on this account as an item to be considered in rate determinations may be supportable but it appears unjustifiable to bar depreciation on this item altogether. Where the property is withdrawn from service for any portion of its life, upon its final retirement, the depreciation reserve set up for it would be inadequate. This can be adjusted by charging the depreciation to surplus rather than as a current account. Thus a true reflection of the adjusted value of the property would be obtained, and yet the accounts will so set off the item that it may be excluded from consideration as a current expense for rate purposes.

Instruction 21(B)(3) directs a purchaser of property which has been acquired by the prior owner as a contribution, to record the contribution which the seller had received. This is done by crediting account 175 "contributions of telephone plant" and debiting the same amount on the asset side, to account 100.4 "Telephone plant acquisition and adjustment" [Instructions 21(B)(4)]. Since this requirement is in addition to the usual entries covering the purchase, it results in swelling the assets and liabilities by a fictitious entry. It constitutes a double recording of this portion of the transaction. This part of the property is recorded once in the usual record of the transaction, and to require its inclusion a second time is unreasonable. No sufficient reason is advanced for such treatment. The desired record could be made without this inflation by a subdivision of account 100.4. It is unreasonable to require duplication and the plaintiffs are injured in so far as they

are denied a reasonable and true accounting record by this provision.

Instruction 2(b)(1) is also objected to. It provides:

> "All charges to the accounts prescribed in this classification for telephone plant, income operating revenues, and operating expenses, shall be just and reasonable and any payment by the company in excess of such just and reasonable charges shall be included in account 323 Miscellaneous income charges."

The information this requirement makes available is essential to any determination of reasonable rates within 201(b) of the Act [ch. 1(4-5) of the Interstate Commerce Act] since they are directly affected by such charges. In the present system, instruction 22 (10)(a) stipulates that the telephone plant accounts be charged with "reasonable amounts" for interest during construction period." The concept is no more indefinite there than the one more widely applied in the proposed system. The idea of "reasonable" is old in the fixation of public utility rates and every rate determination involves consideration of charges here made subject to a distinction between reasonable and unreasonable. Although in isolated cases the question may be very close, generally the classification will not be impossible. As an accounting measure merely, the rule cannot be regarded as beyond the Commission's power.

Exception is also taken to the rule as requiring obedience to a standard as vague and indefinite as to be unconstitutional within the doctrine announced in *United States* v. *Cohen Grocery* (255 U. S. 81); *Tedrow* v. *Lewis & Son Co.* (255 U. S. 98), and *A. B. Small Co.* v. *American Sugar Refining Co.* (267 U. S. 233). First, it appears that the requirement that profits on transactions involving necessaries should not be unjust or unreasonable is without the specialized content of the word "reasonable" with regard to charges involved in the determination of rates. This serves to distinguish the plaintiffs' other cases. Cf. *Connally* v. *General Construction Co.*, 264 U. S. 385; *Cline* v. *Trink Dairy Co.*, 274 U. S. 445; *Champlin Refining Co.* v. *Oklahoma Corp. Commission*, 286 U. S. 210. Second, telephone

companies need incur no risk since those occasional cases which may be doubtful can be submitted for approval under § 220(g) of the act and instruction 9 of the order. To the claim that the Commission is likewise without a standard for judgment, the answer is that the concept of "reasonable" is traditionally defined in utility regulation with sufficient certainty.

The necessity of this order becomes apparent upon consideration of the interrelations of telephone companies. License agreements between subsidiaries can furnish examples of charges clearly not "just and reasonable." Yet any exact definition would be objectionable as arbitrary.

Furthermore, these items, in being subject to interpretation by the Commission and definition as applied to specific facts, are sufficiently definite to guide the Commission. Cf. *Pennsylvania Co.* v. *United States*, 236 U. S. 351, 361; *Interstate Commerce Comm.* v. *Alabama Midland Ry.*, 168 U. S. 144, 170.

It is required that the capital stock expense be set up in account 134.2 which falls in the general class of "Prepaid Accounts and Deferred Charges." 134.2(c) provides that the amortization of this account shall be accomplished by charges to "Miscellaneous debits to surplus." Instruction 20(a) states that the telephone plant accounts, 201-277, shall include the general expense of organization of the accounting company. While the system may appear to be inconsistent in this respect, Montgomery, Auditing Theory & Practice [5th Ed. 1934] p. 416, endorses the write-off of organization expenses to charges against earned surplus, and this would be not unreasonable in view of the accountant's differences on the point. See Paton Accountant's Handbook [2nd Ed. 1934] p. 42.

If inconsistency exists, it may be corrected by the Commission before this requirement can be enforced. What we say must not be regarded as an endorsement of the indiscriminate exclusion of these expenses from the rate base. See *Ohio Utilities* v. *Pacific Utilities Comm.*, 267 U. S. 359. Nor does it mean that expenses of stock flotations subsequent to organization are always necessarily to be regarded as organization expenses.

Except as indicated herein in connection with the depreciation for plant and equipment held for future use, and contributions, the injunction herein prayed for must be denied, but a decree will be entered restraining the enforcement of the instructions given as to these two items.

A decree for plaintiffs as limited in this opinion, may be entered.

February 18, 1936.

MARTIN T. MANTON,
Circuit Judge;
AUGUSTUS N. HAND,
Circuit Judge;
JOHN C. KNOX,
District Judge.

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CHARLES ELMORE CROPLEY
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IN THE

Supreme Court of the United States

OCTOBER TERM 1936.

No. 74.

AMERICAN TELEPHONE & TELEGRAPH COMPANY, *et al.*,
Appellants,

against

UNITED STATES OF AMERICA, FEDERAL COMMUNICATIONS COMMISSION, *et al.*,
Respondents.

BRIEF FOR ADDITIONAL APPELLANTS.

ALLEN T. KLOTS,
Solicitor for Additional Appellants.

HAYDEN N. SMITH,
G. SCHUYLER TARBELL, JR.,
Of Counsel.

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IN THE

SUPREME COURT OF THE UNITED STATES,

OCTOBER TERM 1936

No. 74.

AMERICAN TELEPHONE & TELEGRAPH COMPANY, *et al.*,
Appellants,
against
UNITED STATES OF AMERICA, FEDERAL COMMUNICATIONS COMMISSION, *et al.*,
Respondents.

BRIEF FOR ADDITIONAL APPELLANTS.

Opinion Below.

The opinion of the District Court (R. 561) is reported in 14 Fed. Supp. 121.

Jurisdiction.

This is an appeal from the final decree of a specially constituted District Court for the Southern District of New York. The decree was entered March 24, 1936 (R. 584). The petition for appeal was filed and allowed April 6, 1936 (R. 586-596). Additional appellants have complied with paragraph 1 of Rule 12 by filing a statement of the grounds on which the jurisdiction of this Court is invoked.

Questions Presented.

The main question presented is the validity of the Order of the Federal Communications Commission issued June 19, 1935 entitled "Telephone Division Order No. 7-C" prescribing a Uniform System of Accounts for telephone companies to take effect January 1, 1936 and in particular certain provisions thereof. We contend that certain provisions of this Order and the System prescribed thereby are so arbitrary and unreasonable as to be invalid, beyond any power conferred by statute upon the Commission, and deny the right to keep a true set of accounts in violation of the Fifth Amendment to the Constitution of the United States, and furthermore that these certain provisions are not severable from the system as a whole and invalidate the system as a whole.

In particular the provisions which are assailed are the so-called "original cost" provisions because:

1. They require that the difference between the amount paid for telephone property acquired by the accounting company from a prior owner and the cost to the original owner be treated wholly differently from the balance of the cost and be placed in an "Acquisition Adjustment" account to be disposed of, written off or provision made for the amortization thereof in such manner as the Commission may direct.

2. They fail to provide for or permit any charges for depreciation on the items placed in said Acquisition Adjustment account.

These provisions are to be found in the Uniform System of Accounts prescribed by the Order as follows:

Paragraph 100.1
Paragraph 100.2
Paragraph 100.3

Paragraph 100.4 (R. 122-124)
Instructions 80 and 82 (R. 118-120)
Instructions 20 and 21 (R. 107, 108)
Instructions 3.S.1 (R. 101)

A further question presented is the validity of instructions contained in said Uniform System of Accounts 2(b)(1) requiring that all outlay for plant and operating expenses shall be reasonable and any payments in excess of reasonable amounts shall be charged against income. This is coupled with a statutory provision that punishes as a criminal offense any failure to keep the accounts as prescribed.

The other provision objected to is that which excludes from Account 100.3, covering "Property Held for Future Telephone Use," property not held for "imminent" use, and requires it to be placed in Account 103, "Miscellaneous Physical Property," the depreciation, taxes and maintenance charges on which are not allowed in computing net operating income.

We contend that if the word "imminent" has its usual meaning, i. e., "immediate," the regulation is void, as arbitrary, and if it has not that meaning, it is so vague as to be no guide to accountants and no rule, the disposition of each item of property held for future use being subject to the discretionary dictation of the Commission, and that such treatment is outside of the authority given by the statute, which is to prescribe a uniform system of accounts.

Statement.

The parties on whose behalf this brief is submitted and who are herein sometimes referred to as "additional appellants" are the following telephone companies:

Ohio Associated Telephone Company
Indiana Associated Telephone Corporation
Michigan Associated Telephone Company
Southwestern Associated Telephone Company

Interstate Telephone Company
Tri-State Associated Telephone Corporation
Pennsylvania Telephone Corporation

These seven companies are all independent of the appellant American Telephone & Telegraph Company and the so-called "Bell System". They intervened in this proceeding pursuant to the provisions of the Code of Laws of the United States, Title 28, Section 45a, Judicial Code Sections 212, 213 as amended, and an order of the United States District Court for the Southern District of New York, dated December 6, 1935 (R. 221, 237).

This suit was instituted to enjoin the enforcement of an order of the Federal Communications Commission issued June 19, 1935 entitled "Telephone Division Order No. 7-C" prescribing a Uniform System of Accounts for telephone companies to take effect January 1, 1936 (R. 85-220). The suit was originally commenced by the American Telephone & Telegraph Company and twenty-six other telephone companies in the Bell System. Numerous other companies, including these seven additional appellants, shortly thereafter filed bills of complaint and intervened in the suit. The case was heard before a specially constituted District Court on a motion of the plaintiffs for a temporary restraining order and an interlocutory injunction (R. 306). At the conclusion of the hearing the parties stipulated to submit the case for final decree as well as for a temporary restraining order and interlocutory injunction upon the pleadings and affidavits (R. 552). The decision of the District Court was handed down on February 18, 936 (R. 561) and the decree entered March 24, 1936 (R. 584). The District Court permanently enjoined the enforcement of two provisions of the Commission's Order, but refused to enjoin certain other provisions of which the plaintiffs complained and the invalidity of which it was also claimed invalidated the entire Order.

The provisions of the Communications Act of 1934, Act of June 19, 1934, Ch. 652, 48 Stat. 1078, 47 U. S. C. § 220, which gave the Commission power to prescribe forms of account are as follows:

> "Sec. 220(a). The Commission may, in its discretion, *prescribe the forms* of any and all accounts, records, and memoranda to be kept by carriers subject to this Act, including the accounts, records, and memoranda of the movement of traffic, as well as of the receipts and expenditures of moneys.
>
> (b) The Commission shall, as soon as practicable, prescribe for such carriers the classes of property for which depreciation charges may be properly included under operating expenses, and the percentages of depreciation which shall be charged with respect to each of such classes of property, classifying the carriers as it may deem proper for this purpose. The Commission may, when it deems necessary, modify the classes and percentages so prescribed. Such carriers shall not, after the Commission has prescribed the classes of property for which depreciation charges may be included, charge to operating expenses any depreciation charges on classes of property other than those prescribed by the Commission, or, after the Commission has prescribed percentages of depreciation, charge with respect to any class of property a percentage of depreciation other than that prescribed therefor by the Commission. * * *
>
> (d) In case of failure or refusal on the part of any such carrier to keep such accounts, records, and memoranda on the books and in the manner prescribed by the Commission * * * such carrier shall forfeit to the United States the sum of $500.00 for each day of the continuance of each such offense.
>
> * * * * *
>
> (g) After the Commission has prescribed the forms and manner of keeping of accounts, records, and memoranda to be kept by any person as herein provided, it shall be unlawful for such person to keep any other accounts, records, or memoranda than those so prescribed or such as may be approved by

> the Commission or to keep the accounts in any other manner than that prescribed or approved by the Commission. Notice of alterations by the Commission in the required manner or form of keeping accounts shall be given to such persons by the Commission at least six months before the same are to take effect." (Italics ours.)

The provisions of the Uniform System prescribed by the Commission to which the argument in this brief will be primarily directed are the so-called "original cost" provisions. These provisions require that the plant investment accounts of a telephone company shall be divided into four main accounts as follows:

Account 100.1	Telephone Plant in Service
Account 100.2	Telephone Plant under Construction
Account 100.3	Property Held for Future Use
Account 100.4	Telephone Plant Acquisition Adjustment (R. 122, 123).

They then provide that in the *first three* of these accounts shall be entered only the so-called "original cost" of the property in question. "Original cost" is defined by Instruction 3.S.1. in said System as

> "The actual money cost of (or the current money value of any consideration other than money exchanged for) property at the time when it was first dedicated to the public use, whether by the accounting company or by a predecessor public utility." (R. 101.)

In other words, it is provided that into *these three* accounts there shall be entered in the case of property which has been purchased by the accounting company not the cost to the accounting company of such property, but the cost to the party which first dedicated it to the public use. Depreciation is allowed on depreciable items entered in these three accounts and they are in other respects treated by the System as normal plant accounts.

The balance of the actual cost to the accounting company of purchased telephone plant is ordered to be entered in Account 100.4 as "Telephone Plant Acquisition Adjustment". This account is treated quite differently from the normal plant accounts. It is provided in paragraph (C) of said Account 100.4 (R. 124) that

> "The amounts recorded in this account in respect to each property acquisition shall be disposed of, written off, or provision shall be made for the amortization thereof in such manner as this Commission may direct."

There is no rule or principle prescribed for disposing of the items in this Account No. 100.4.

It will then be discovered by examining paragraph 82, "Classes of Depreciable Telephone Plant" (R. 120) and paragraph 80 (R. 118) that no depreciation is permitted to be charged on the items contained in this account.

These "original cost" provisions apply not only to property hereafter acquired, but are retroactive in the sense that appellants are required to set up their books on this new plan even in respect to properties heretofore acquired. This makes the Order and System prescribed peculiarly burdensome upon these additional appellants because of the nature of their properties. These properties were practically all acquired from predecessor owners (R. 583). There were at least 233 of such predecessors (R. 583). In most instances additional appellants' immediate predecessors had in turn acquired these properties from former owners. These properties are located for the most part in small rural communities. Only two of the approximately 669 communities served have more than one telephone exchange (R. 459). The former owners who originally built the telephone lines consisted of small companies or individuals and in many cases farmers mutual associations. The records of the additional appellants' immediate predecessors were in almost every case inadequately and inaccurately kept and were themselves in turn based upon purchases of going businesses

from their predecessors. In many instances no records at all were kept by the companies, individuals or farmers mutual associations who originally built the telephone lines and plant and in many other cases their books or records are not now available, or if available are known to be inaccurate (R. 459-460, 462-467, 583).

"Original cost" provisions of a similar character adopted by the New York Public Service Commission have been held invalid under the laws and Constitutions of the State of New York and of the United States of America by the New York Court of Appeals in *Matter of New York Edison Company, et al.* v. *Maltbie,* 271 N. Y. 103. See also opinion of the Appellate Division of the Supreme Court, 244 N. Y. App. Div. 685.

The provisions herein assailed were urged upon the Interstate Commerce Commission by certain state commissions led by the Public Service Commission of New York (R. 15, 17). In July, 1934, the Interstate Commerce Commission rendered a report upon these various recommendations after numerous hearings at which representatives of the commissions and other companies appeared (R. 15). This report did not take the form of an order because the jurisdiction of the Interstate Commerce Commission in the matter was subsequently superseded by that of the Federal Communications Commission (R. 84). The Interstate Commerce Commission definitely rejected the proposal for such "original cost" provisions (R. 57, 83).

The Michigan Public Utilities Commission has rejected this very System by an order No. D-1140 dated December 3, 1935, effective January 1, 1936.

The Public Service Commission of Wisconsin by order No. 2-U-902 dated December 20, 1935 has rejected the treatment accorded to Telephone Plant Acquisition Adjustment Account, No. 100.4, and required that items in this account which consist of a portion of the cost of depreciable property be depreciated and appropriate depreciation reserve accounts set up.

Specification of Errors.

1. The District Court erred in refusing to enjoin the provisions of the Commission's Order respecting "original cost", particularly in so far as it requires the difference between the amount paid for property by the accounting company and the cost to some prior owner to be entered in the "Acquisition Adjustment" Account to be disposed of, written off or provision made for the amortization thereof in such manner as the Commission may direct (Assignments of Error, Nos. 1, 2, 3, 4, 5, 6, 7, 8 and 9, R. 587-589).

2. The District Court erred in refusing to enjoin the provisions of the Commission's Order respecting "original cost" in that they failed to provide for or permit charges for depreciation on the items placed in "Telephone Plant Acquisition Adjustment" Account (Assignments of Error, Nos. 4, 5, 6, 26, 28, R. 589, 592).

3. The District Court erred in refusing to enjoin the enforcement of Instruction 2(b)(1) respecting just and reasonable outlay for property or expenses (Assignments of Error, Nos. 10, 11, 12, 13, 14, 34, R. 590, 593).

4. The District Court erred in refusing to enjoin the enforcement of the provisions for classification of physical property, including particularly the classification based on "imminent" use, and the requirement that property not held for "imminent" future use should be placed in Account 103, Miscellaneous Physical Property (Assignments 14-18, R. 590-1).

5. The District Court erred in refusing to enjoin the enforcement of the whole Order, on the ground that the invalid provisions above mentioned and those it held void are inseparable from the rest and what remains is an incomplete and unworkable system of accounts (Assignments of Error, Nos. 20, 21, 22, 35, R. 591-593).

This brief will be devoted primarily to the argument of certain aspects of our "original cost" contentions. We endorse in addition the arguments made by the other appellants on the same point. We do not abandon the other errors hereinabove specified, but endorse the contentions of the other appellants in regard thereto and will refrain from burdening the Court with a repetition thereof.

Summary of Argument.

1. The right to keep a reasonable and adequate set of books is one which is recognized and protected by the courts and a denial of this right constitutes forthwith and immediately irreparable injury to these appellants. The "original cost" provisions violate this right of these appellants because they prescribe a system of accounts which is capricious, arbitrary, unfair and misleading. They require the segregation of a portion of the actual cost of acquired property into an account separate from the legitimate property accounts and characterize it as subject to treatment which has no basis either in fact or in the power of the Commission.

2. The statute requires the Commission to prescribe the classes of depreciable property. It is obviously intended that accounts shall be provided for each depreciable item on the company's books. Instead of doing this it has required depreciable items to be placed in Account 100.4—a non-depreciable account—and has provided no depreciable account for such items.

ARGUMENT.

I.

The original cost provisions are void because they are capricious, arbitrary, unfair and misleading.

A.

The right to keep a reasonable and adequate set of books is one which is recognized and protected by the courts.

Yu Cong Eng v. *Trinidad*, 271 U. S. 500;
Norfolk & Western Railway Co. v. *U. S.*, 287 U. S. 134, 143;
Kansas City Southern Railway Co. v. *U. S.*, 231 U. S. 423, 440;
Chesepeake & Ohio Ry. Co. v. *U. S.*, 5 Fed. Supp. 7, 10.

To deny by arbitrary and unreasonable requirements this right so indispensable to the proper conduct of any business, constitutes *forthwith* and *immediately* an injury to the appellants and requires no further action or fruition to make the damage complete.

B.

The "original cost" provisions prescribed by this Order are arbitrary and unreasonable not only because they are capricious but because in addition they result in false and misleading accounts. The fundamental vice of the system is that it segregates part of the actual cost to the accounting company of tangible telephone property into a separate account, to wit: Telephone Plant Acquisition Adjustment Account, No. 100.4, which is not accorded the treatment that a legitimate property account is entitled to. This segre-

gation and separate treatment is justified by nothing inherent in the items which are required to be put into this account. It is based on the wholly unfounded theory of the Commission that only the "original cost" is the figure to be included in the legitimate property accounts of the company.

The Telephone Plant Acquisition Adjustment Account is in its essence a suspense account, the items of which are subject to be disposed of, written off or amortized as the Commission may direct. Now there is no fact implicit in the genesis of the items which are to be placed in this account which makes them appropriate or qualified for any such classification. The items that go into this account go into it merely because they happen to be the difference between what the accounting company paid for the property and the so-called "original cost". This is their only determinant, but this fact is no criterion of whether they are to be written off or that they are to be amortized rather than depreciated, or, indeed, that they should be disposed of in any way different from the balance of the cost to the accounting company which goes into Accounts 100.1, 100.2 and 100.3. To require this classification and segregation of part of the actual cost for no reason whatever is thus capricious in the highest degree. It represents not only arbitrary action, but arbitrary action without any basis that is even colorably sound.

But more important, it is unfair, misleading and false. The implication is at once given that the items in Telephone Plant Acquisition Adjustment Account, 100.4, represents something intangible or unjustifiable write ups; that they are not entitled to have set up the usual depreciation reserve to which tangible assets in service are entitled and that they are subject to be written off out of surplus and the company required to take a loss in respect to them if the Commission so directs. The impression thus created by the requirement of this account, upon investors, security holders, ratepayers,

regulatory bodies or any other persons having occasion to examine the balance sheet of the company is false because:

1. The items in this account do represent actual assets devoted to the public use. Until there has been an adjudication in some sort of a proceeding such as a rate proceeding after a hearing on the specific issue that some part of the cost to these plaintiffs of property purchased represents excessive valuation, the amount actually paid by these plaintiffs for the property cannot thus be summarily impeached as representing a doubtful portion of the value of the asset. In most cases, as previously stated, the purchase of the asset at this price was approved by a state public service commission (R. 462-465). Certainly the price thus paid is a better criterion of the value of the property than a so-called "original cost" resurrected partly from incomplete and inaccurate records of the past and partly from pure estimate and conjecture. In the case of these particular appellants, for example, the original cost of the following portions of their entire properties will have to be estimated to the following extent:

Interstate Telephone Company.....	80%	R. 463
Michigan Associated Telephone Company	80%	R. 464
Ohio Associated Telephone Company...	75%	R. 465
Pennsylvania Telephone Corporation...	54%	R. 466
Tri-State Associated Telephone Corporation	50%	R. 466
Southwestern Associated Telephone Company	substantially more than half	R. 467
Indiana Associated Telephone Company..	substantial portion	R. 462

2. The implication that the items in this account are not entitled to be depreciated or to a depreciation reserve is also false. The Commission has not the power to deny to the company the right to set aside a depreciation reserve for these items, arbitrarily and solely on the basis that they happened to constitute an excess over the cost to the original owner.

In the case of *Knoxville* v. *Knoxville Water Company*, 212 U. S. 1, at page 13, the Supreme Court said:

> "It (the company) is entitled to see that from earnings the value of the property invested is kept unimpaired, so that at the end of any given term of years the original investment remains as it was at the beginning. It is not only the right of the company to make such a provision, but it is its duty to its bond and stock holders, and, in the case of a public service corporation at least, its plain duty to the public."

There is certainly no case in the books which holds that the investment which is to be kept unimpaired is the investment *of somebody else* rather than the investment of the accounting company.

By providing in this order that these items are non-depreciable, the Commission has assumed to prejudge them without a hearing as non-recoverable to any extent out of earnings, to set them apart with a stigma upon them, and thus without justification in fact or in law to cast doubt upon plaintiffs' whole property account.

3. The implication that these items are subject to be disposed of, written off or amortized as the Commission may direct is false and misleading. The term "written-off" as used in this provision was primarily intended to mean written off out of surplus, that is to say, taken as a loss and destroyed as an asset of the company. It is quite evident from the Order and System as a whole that this is the intended disposition of most of this account and anyone reading the Order and System prescribed would so assume. This implication is false and misleading because the Commission has no power to require these appellants to write off and take as a loss a part of what they actually paid for their property. There is nothing in the statute authorizing them to do this. The Commission's right to

determine a rate base does not either directly or by implication give it the power thus to deal with the company's investment. Certainly under the guise of prescribing a uniform system of accounts and as incidental thereto, the Commission has no right to require these plaintiffs to take a loss or to record on their books a loss which they have not actually suffered.

People ex rel. Iroquois Gas Corporation v. *Public Service Commission,* 264 N. Y. 17.

The New York Court of Appeals held and said in that case as to the power of the New York Public Service Commission, at page 21:

> "The power vested in the Commission to prescribe uniform methods of keeping accounts and records (Pub. Serv. Law, section 66, subd. 4), does not include the power to compel a corporation to write off from its book value a loss which it has not sustained, or to give up a part of its constitutional rights. If, as has been said, 'the actual cost of the property—the investment the owners have made—is a relevant fact' (Los Angeles Gas and Elec. Corp. v. Railroad Comm., 289 U. S. 287, 306) a corporation cannot be compelled to make entries upon its books calculated to conceal such relevant fact. It follows that the commission had no power to impose such condition."

The Commission's rate making power and its power to deny appellants the right to keep adequate and accurate accounts must, throughout this case, be carefully distinguished. We are not considering in this case the power of the Commission in determining rates to direct that a certain portion of the cost be disregarded. We are discussing the right of the Commission under the guise of prescribing "forms of account" to require these companies to write off from their books a loss which they have in fact not suffered. The Commission has no such power and a balance sheet

which labels a substantial part of the assets as subject to the exercise of such power is, therefore, false, inaccurate and misleading.

C.

If we assume for the sake of argument a balance sheet set up in the manner required by the Commission, we see the falsity in which it immediately results and the arbitrary and capricious nature of the order requiring such a balance sheet. Suppose Company XYZ acquired practically all of its telephone plant from predecessor companies and paid $1,000,000. for it. The balance sheet required by the Commission's Order would look something like this:

Assets		*Liabilities*	
Telephone Plant in Service (Acct. 100.1)	$ 700,000.00	Capital Stock...	$ 400,000.00
Telephone Plant Under Construction (Acct. 100.2)	50,000.00	Bonds	600,000.00
Property Held for Future Use (Acct. 100.3)	50,000.00	Other liabilities.	100,000.00
*Telephone Plant Acquisition Adjustment (Acct. 100.4)	200,000.00	Surplus (See Notes 1 and 2)	100,000.00
Other assets	200,000.00		
	$1,200,000.00		$1,200,000.00

*Note 1: Not subject to depreciation.

*Note 2: Subject to be disposed of, written off or provision made for the amortization thereof in such manner as the Commission may direct.

Looking at the above balance sheet it will appear that part of the actual cost of $1,000,000. to the XYZ Company of its plant in service has been removed from the physical plant accounts and put in the account labeled "Telephone Plant Acquisition Adjustment". There is no evidence either in the record or before the Commission that the portion of the cost represented by the $200,000. item is not just as much a legitimate part of the actual value of that property *for all purposes* as the $800,000. in the three preceding accounts. It being the price actually paid and there being

no presumption that the purchase was not one freely negotiated at arm's length, it is certainly important evidence of value at that time. In addition, in most instances it has been approved by some state commission (R. 462-465). There is no evidence that it represents improper write-up, water or any other inflated element of value. Certainly *prima facie* it is a much more reliable criterion of value than would be the guess as to what it may have cost a group of farmers mutual associations, which had no books and never had any books, which built the lines originally. Yet the only thing we are permitted to set up in our books and label as actual telephone plant in service or under construction or held for future use *is this estimate or guess.* The balance of the actual cost to us, namely the $200,000., we are required to submit to the stigma of this label.

Although the figures in the above example are fictitious and chosen solely for the sake of illustration, the notes indicated by an asterisk are by no means supposititious or imaginary. Honest accounting would seem clearly to require them. Thus Dean Madden of New York University in his affidavit says:

> "A balance sheet which would fail to call specific attention on its face to the fact that the Commission *must* extinguish this item and *may* extinguish it immediately by a write off is incomplete and misleading, and not in accordance with correct accounting principles." (R. 320).

The mere title of the account, "Telephone Plant Acquisition Adjustment" in itself casts a cloud of suspicion on the items and removes them from the category of tangible assets. When in addition these items are labeled as non-depreciable their impending doom as tangible assets is at once implied. Finally when they are labeled as subject to be written off or otherwise disposed of as the Commission may direct, the implication that their doom is sealed is irresistible. *And yet all these implications are false because*

they have no basis either in fact or in the power of the Commission!

In estimating the harm that results *immediately* and *forthwith* to the appellants, their stockholders and bondholders, by requiring the adoption of such misleading and false accounts and balance sheets, it is also to be remembered that investors in their securities invested on the faith of the balance sheets and accounts heretofore issued and kept by these companies in accordance with the requirements of the Interstate Commerce Commission, which show the true facts as to the actual cost to these appellants of the properties purchased and truthfully include this item in such cost. By merely looking at the sample balance sheet above set out, the disastrous result to the company's surplus of the segregation and earmarking as dubious of a part of the assets, heretofore legitimately carried as property of real substance, can at once be seen as well as the effect upon the value of its capital stock and even on its first mortgage bonds. This result is entirely unwarranted by any facts on which this harmful segregation is predicated. To impose a requirement which achieves such an unwarranted, false and misleading result is totally arbitrary and unreasonable.

D.

A comparison of Account 100.4 with Account 278 in the System now in effect prescribed by the Interstate Commerce Commission brings into sharp relief the wholly capricious nature of Account 100.4, as prescribed by this Order. The respondents have argued that Account 100.4 is of the same nature and performs the same functions as Account 278 and the Court below indicated this in its opinion (R. 567). The fact is, however, that the genesis of the items which go into Account 278 has a reasonable and proper relation to the function of this account, whereas the genesis of the items which go into Account 100.4 has no such relationship in fact or in law. Account 278 is arrived at under the System now in effect as follows:

When a going telephone property is acquired, so much of the purchase price as equals the current cost new of the various items of tangible property, except land, is carried in appropriate depreciable asset accounts. Land is carried in a separate account at estimated current value. The original cost of franchises is set up in another appropriate asset account. The balance, which will thus in real measure represent the amount in fact paid for the intangible or going value of the properties purchased, is placed in Account 278 (R. 404). Because of the intangible nature of the property thus put into Account 278 it is properly not subject to a depreciation charge. In other words; the determination of the items which go into Account 278 has a logical basis founded in law and fact in that property items properly non-depreciable are segregated into a non-depreciable account.

Account 100.4, as defined in the System complained of, however, has no such logical basis for separate classification, but on the contrary involves a wholly arbitrary and artificial segregation of part of the actual amount paid by the accounting party for each item of tangible depreciable property purchased. The difference between what the accounting party paid for the property and the original cost does not represent the amount paid for the intangible non-depreciable portion, if any, of the property purchased and is no measure thereof. To say that the excess paid over the cost to somebody else in the past is *ipso facto* or even *prima facie* paid for intangible good will or "going concern" value and is non-depreciable, disregards changes in true value due to changes in price level or other factors and has no foundation in logic or fact.

II.

The order is invalid because it has not provided any depreciable classification for certain items of tangible property clearly subject to depreciation.

By subdivision (b) of that Section of the Act which authorizes uniform accounts (Section 220), the Commission is required to prescribe the classes of property for which depreciation charges may be properly included under operating expenses. This provision of the statute reads as follows:

> "(b) The Commission shall, as soon as practicable, prescribe for such carriers the classes of property for which depreciation charges may be properly included under operating expenses, and the percentages of depreciation which shall be charged with respect to each of such classes of property, classifying the carriers as it may deem proper for this purpose. The Commission may, when it deems necessary, modify the classes and percentages so prescribed. Such carriers shall not, after the Commission has prescribed the classes of property for which depreciation charges may be included, charge to operating expenses any depreciation charges on classes of property other than those prescribed by the Commission, or, after the Commission has prescribed percentages of depreciation, charge with respect to any class of property a percentage of depreciation other than that prescribed therefor by the Commission. No such carrier shall in any case include in any form under its operating or other expenses any depreciation or other charge or expenditure included elsewhere as a depreciation charge or otherwise under its operating or other expenses."

In requiring the Commission to prescribe "the classes of property for which depreciation charges may be properly included under operating expenses" the statute undoubtedly

intended that the Commission should provide depreciable property accounts for *all* items representing depreciable property. The Commission has assumed to do this and in paragraph 82 of the Instructions has listed them (R. 120). On no other account or classification of property is depreciation permitted to be taken either as a charge to operating expenses or to any other accounts. No part of the items recorded in Account 100.4, however, is included in any of the depreciable accounts listed in paragraph 82 of the Instructions. These accounts are all sub-accounts of "Telephone Plant in Service" account, No. 100.1, into which is permitted to be entered only the "original cost" (R. 122).

Yet many of the items required to be placed in Account 100.4 are most certainly entitled to depreciation. As has already been indicated in the previous point, there is nothing in the genesis of the items in Account 100.4 which makes any of them non-depreciable. On the contrary, they represent a substantial portion of the cost of tangible depreciable property to the accounting company. *Prima facie* they are entitled to depreciation chargeable against operating expenses. Yet no depreciable account has been provided into which any of them may be put.

In failing to classify the items in Account 100.4 or any part thereof as depreciable the Commission has, therefore, omitted a substantial classification or classifications in its list of depreciable accounts. This Order which assumes to prescribe the complete set of depreciable accounts as directed by the statute, has thus omitted certain accounts which the Commission was directed by the statute to include therein. It is, therefore, vitally defective and invalid.

But the Commission argues that it still may permit appellants to depreciate some of the items required to be placed in Account 100.4 if requested individually item by item. The first answer to this is that the Commission has already assumed to name the classes of depreciable property and has excluded all items in Account 100.4 from these classes. No mention is made in the Order or any indication given that

any part of Account 100.4 is to be regarded as depreciable. Nor is any account provided into which these items could be put if ultimately so held. This Order was made, moreover, after numerous hearings, first before the Interstate Commerce Commission and then before this defendant Commission and when the Order was finally made no depreciable classification was provided for the items in Account 100.4. Appellants have a right under the statute to a depreciable classification for depreciable items and not merely a right to be afforded the opportunity to ask the Commission item by item that depreciation be permitted. The Commission's power in turn is limited by the statute to prescribing classifications.

Under the Commission's argument it could have placed the entire cost of acquired property in Account 100.4 and placed none of it in the depreciable plant accounts. Would this have been a justifiable classification? Would it have been an answer to the failure to provide a depreciable account for any part of the cost of acquired property that the company could have gone and asked them item by item to permit depreciation on such items? Or suppose the Commission had provided that all red telephone poles should be put in depreciable account 100.1 but that all green telephone poles should be put in account 100.4. Would this have been a reasonable classification because of the Commission's offer to permit us to request a separate order for depreciation as to each pole placed in Account 100.4? And yet there is no more reason for distinguishing between the "original cost" of and the balance paid for, acquired property than between red telephone poles and green telephone poles.

Finally, if we should accept the Commission at its word, submit to the Order as it now stands and then petition the Commission to allow us to depreciate tangible assets of these companies devoted to the public use, and we were then met with a ruling denying our petition, in accordance with certain recognized principles laid down by this Court, such a

ruling might well constitute a negative order not subject to court review.

Proctor and Gamble Company v. *U. S.*, 225 U. S. 282;
Lehigh Valley R. R. Co. v. *U. S.*, 243 U. S. 412;

See

Scharfman, The Interstate Commerce Commission, Vol. II, pages 406-417.

In other words, this proceeding may well be our last clear chance to obtain a judicial review of this ruling of the Commission as to depreciation.

The company cannot be denied the right to set up a depreciation reserve as to its investment in tangible property subject to depreciation in fact. It is elementary that provident management demands that a company shall preserve its property investment by taking out of its revenues each year an amount equivalent to the amount by which it is calculated to have depreciated and not been replaced by maintenance. This is the management's plain duty to its bondholders and stockholders who have supplied the funds for that investment. Its right to do this under the Constitution is fully sanctioned by judicial authority.

Knoxville v. *Knoxville Water Co.*, 212 U. S. 1, 13-14;
United Railways v. *West*, 280 U. S. 234, 253.

This principle has nothing to do with the computation of a rate base or the determination of fair and reasonable rates. Whether the full amount of the depreciation taken should be deducted in computing a fair return for the purpose of rate making is another question entirely. It may be that a provident management will require that the amount allowed as a fair return in a rate case shall be cut down by self imposed charges for depreciation not considered in such case. This it has a right to do. It has this right—yea,

duty—to protect the capital investment of its bondholders and stockholders. But this Order forbids the management to do this. What was paid for the tangible property subject to wear and tear is their capital investment in such property and to preserve this capital, depreciation reserves must be set aside out of revenues proportionate to that investment—not proportionate to someone else's investment. This principle has nothing to do with the rates. It does not affect rates, but it is vital to sound management and sound bookkeeping and the Commission cannot lawfully interfere with these.

The power to prescribe uniform forms of account does not include the power to interfere with the management of a company in the direction of its finances or to regulate the management of a company's finances. As was said by the New York Court in the case of *Matter of New York Edison Company* v. *Maltbie,* 244 App. Div. 685, at page 687 (aff'd 271 N. Y. 103):

> "The statute does not authorize the commission to prescribe uniform methods of management of the business of privately owned corporations. The uniformity that may be enforced is not as to what shall be done or how it shall be done, but as to book entries in respect to whatever is done."

In the case of *People ex rel. New York Railway Company* v. *Public Service Commission,* 223 N. Y. 373 the Court of Appeals said at page 378:

> "By establishing a system of accounts the corporations were required to show under particular heads what they had done. It was not to regulate the management of their finances but to show what the management was."

See also:

Passaic Consolidated Water Co. v. *Board of Public Utility Commissioners,* 5 N. J. M. 1078, 139 Atl. 324; aff'd 104 N. J. L. 666, 141 Atl. 921 (N. J. 1927);

Havre de Grace and Perryville Bridge Company v. *Towers,* 132 Md. 16, 103 Atl. 319, 321 (Md. 1918);

Southwestern Telephone Co. v. *Public Service Commission,* 262 U. S. 276, 289.

III.

The provisions of the order and system complained of are not severable and the order and system as a whole should be annulled and set aside and the enforcement thereof enjoined.

The System prescribed by the Commission purports to constitute a complete system of accounts and its various provisions are interlocking and supplementary to each other to a very large extent. With the elimination of the provisions complained of here and the provisions enjoined below it seems to us that this System is unworkable and a very extensive modification and revision would be necessary to constitute a practicable working system. Its invalidity as a whole must therefore be declared and its enforcement in its present form enjoined.

Respectfully submitted,

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Solicitor for Additional Appellants.

HAYDEN N. SMITH,

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1936.

NO. 74.

AMERICAN TELEPHONE AND TELEGRAPH COMPANY, *et al.*,
Appellants,

vs.

THE UNITED STATES OF AMERICA, FEDERAL COMMUNICATIONS COMMISSION and NATIONAL ASSOCIATION OF RAILROAD AND UTILITIES COMMISSIONERS,
Respondents.

BRIEF FOR APPELLANTS, AMERICAN TELEPHONE AND TELEGRAPH COMPANY AND OTHERS.

Opinion Below

The opinion of the District Court (R. 561) is reported in 14 F. Supp. 121.

Jurisdiction

This is an appeal from the final decree of a specially constituted District Court for the Southern District of New York. The decree was entered March 24, 1936 (R. 584). The petition for appeal was filed and allowed April 6, 1936 (R. 586-596). Appellants have complied with paragraph 1 of Rule 12 by filing a statement of the grounds on which the jurisdiction of this Court is invoked.

Questions Presented

This is a suit to enjoin the enforcement of an order of the Federal Communications Commission prescribing a uniform system of accounts for telephone companies. Two of the provisions complained of were enjoined by the District Court and no appeal has been taken by the defendants.

The appellants here urge that three other provisions of the order are void.

1. The first prescribes the method of entering in the books of account purchases from another public utility of property already in use in public service, and requires recasting the books as to all such purchases in the past.

The Commission's order defines the "original cost" of such property as the cost to the company which owned it when first dedicated to the public use, and requires that the accounting company shall enter such "original cost" (estimated if not known) in its property investment accounts.

The difference between the actual or estimated "original cost", and the amount actually paid for the property by the accounting company, is required to be entered in an account labeled "Telephone Plant Acquisition Adjustment", which, the order provides, shall be disposed of, written off or amortized in such manner as the Commission may direct in the case of each separate purchase.

Although annual depreciation of telephone plant is treated as an operating expense entering into the computation of net operating income, the order forbids charging depreciation on the "Telephone Plant Acquisition Adjustment" account as an operating expense.

The appellants contend these provisions are void because:

(a) Broad as the discretion of the Commission may be, under the statute, it has no authority to prescribe a system of accounts which does not truly record the actual condition and actual transactions of a telephone company.

(b) Excluding a part of the cost of property from the investment accounts and placing it in an "adjustment" or suspense account which is subject to be written off immediately or later, in the discretion of the Commission, misstates the true property investment.

(c) Refusing to allow the companies to charge in the operating account annual depreciation on the part of the property cost placed in the adjustment account requires a false statement of net operating income.

(d) The statute authorizes the Commission to prescribe rules in accordance with which all telephone companies, or all within a class, shall keep their accounts. The requirement that part of the cost of property shall be placed in an adjustment account and disposed of, not in accordance with any rule, but as the Commission may direct in the case of each individual property acquisition, is not authorized by the statute.

(e) Accounts which truly record the facts of a company's own actual transactions and condition, such as actual cost of its property, are necessary for the management of its business and for the information of stockholders, prospective investors and tax collectors, as well as for rate making purposes. If additional information as to the transactions of prior owners is deemed helpful in establishing a ratebase, that can be ac-

complished by the use of supplemental records without excluding, as the prescribed system does, a correct record of the company's own transactions.

2. Another provision objected to is that which states all outlay for plant and operating expenses shall be reasonable and any payments in excess of "reasonable" amounts shall be charged against income and ignored in arriving at net operating income. This is coupled with the statutory provisions that punish as a criminal offense and by forfeitures any failure to keep the accounts as prescribed and provide for enforcement by civil process.

We contend that this provision is arbitrary, because it requires the accountant not to record what was paid, but what someone's opinion is as to what should have been paid.

It also is void because it demands obedience to a rule so vague as not to constitute a legal standard of conduct. The statute, punishing criminally failure to obey the order prescribing the form of accounts, contemplates that the order prescribing the forms shall be sufficiently definite so that a violation may be the subject of criminal proceeding. Under the Lever Act cases, applying the 5th amendment, a violation of this requirement could not be punished criminally. Therefore the provision is not authorized by the statute.

3. The third objection is to the classifications prescribed for physical property, as applied to spare plant. These provisions exclude from Account 100.3, covering "Property Held for Future Telephone Use", property not held for "imminent" use, and require it to be placed in Account 103, "Miscellaneous Physi-

cal Property", the depreciation, taxes and maintenance charges on which are not allowed in computing net operating income.

We contend that if the word "imminent" has its usual meaning, *i. e.*, "immediate", the regulation is void, as arbitrary, and if it has not that meaning, it is so vague as to be no guide to accountants and no rule, the disposition of each item of property held for future use being subject to the discretionary dictation of the Commission, and that such treatment is outside of the authority given by the statute, which is to prescribe a uniform system of accounts.

The same objection as to vagueness applies to the provisions which exclude an undeterminable amount of plant from Account 100.1, "Telephone Plant in Service," and require it to be placed in Account 100.3, "Property Held for Future Telephone Use."

The Statute

The provisions of the Communications Act of 1934, approved June 19, 1934 (48 Stat. L. 1064, 1078-1080), which give the Commission power to prescribe the forms of accounts are as follows:

> "Sec. 220. (a) The Commission may, in its discretion, *prescribe the forms* of any and all accounts, records and memoranda to be kept by carriers subject to this Act, including the accounts, records, and memoranda of the movement of traffic, as well as of the receipts and expenditures of moneys." (Italics supplied.)
>
> "(b) The Commission shall, as soon as practicable, prescribe for such carriers the classes of property for which depreciation charges may be properly included under operating expenses, and the percentages of depreciation which shall be

charged with respect to each of such classes of property, classifying the carriers as it may deem proper for this purpose. The Commission may, when it deems necessary, modify the classes and percentages so prescribed. Such carriers shall not, after the Commission has prescribed the classes of property for which depreciation charges may be included, charge to operating expenses any depreciation charges on classes of property other than those prescribed by the Commission, or, after the Commission has prescribed percentages of depreciation, charge with respect to any class of property a percentage of depreciation other than that prescribed therefor by the Commission. * * *

"(d) In case of failure or refusal on the part of any such carrier to keep such accounts, records, and memoranda on the books and in the manner prescribed by the Commission, * * * such carrier shall forfeit to the United States the sum of $500 for each day of the continuance of each such offense.

"(g) After the Commission has prescribed the forms and manner of keeping of accounts, records, and memoranda to be kept by any person as herein provided, it shall be unlawful for such person to keep any other accounts, records, or memoranda than those so prescribed or such as may be approved by the Commission or to keep the accounts in any other manner than that prescribed or approved by the Commission. Notice of alterations by the Commission in the required manner or form of keeping accounts shall be given to such persons by the Commission at least six months before the same are to take effect.

"(h) The Commission may classify carriers subject to this Act and prescribe different require-

ments under this section for different classes of carriers, and may, if it deems such action consistent with the public interest, except the carriers of any particular class or classes in any State from any of the requirements under this section in cases where such carriers are subject to State commission regulation with respect to matters to which this section relates."

Statement

On June 19, 1935, the Federal Communications Commission issued "Telephone Division Order No. 7-C" (R. 91-94) prescribing a Uniform System of Accounts for Telephone Companies, to take effect January 1, 1936 (R. 85-220).

On November 22, 1935, the American Telephone and Telegraph Company, and twenty-eight other telephone companies in the Bell System, brought this suit (R. 1) in the Southern District of New York, to enjoin the enforcement of the order. On December 6, 1935 (R. 222) seven other telephone companies filed a bill of complaint and were allowed to join in the suit (R. 237) as additional plaintiffs. Eight additional telephone companies intervened on December 16, 1935 (R. 240). The National Association of Railroad and Utilities Commissioners was allowed to intervene as a party defendant (R. 271). The case came on to be heard December 13, 1935, before a specially constituted District Court on the motion of the plaintiffs for a temporary restraining order and an interlocutory injunction (R. 306). At the conclusion of the hearing the parties stipulated (R. 552) to submit the case for final decree as well as for temporary restraining order and interlocutory injunction, upon the pleadings and the affidavits filed and to be filed by the parties, whereupon on December 28, 1935, the Court reserved decision on the motion for interlocutory in-

junction, and granted a stay of the Commission's order pending final decision (R. 559). The additional affidavits having been filed, the Court filed its opinion (R. 561) February 18, 1936, and its findings (R. 572) and decree (R. 584) March 24, 1936. The District Court permanently enjoined the enforcement of two requirements of the Commission's order. One of the requirements enjoined was that which prevented the companies from charging depreciation on that part of their telephone plants in Account 100.3, entitled "Property Held for Future Telephone Use" (R. 585). The system of accounts made no provision for charging depreciation on property in this account, although the time the property remained in this account was required to be included in its total life, on which the annual depreciation rate was based, thus preventing full depreciation from ever being charged. The other requirement enjoined (R. 585) was that which required that when one company had bought telephone property from another telephone company, which property had been received by the predecessor company as a gift or contribution, the purchasing company, notwithstanding it paid cash for the property, was required to record the contribution on its books as a liability (R. 570). The defendants have not appealed from this action of the Court below. All other relief asked for was denied, and this appeal by all the plaintiffs followed.

Beginning January 1, 1913, the accounts of telephone companies have been kept in accordance with a system prescribed by the Interstate Commerce Commission on December 10, 1912, and which, with minor amendments, remained in effect until January 1, 1933, on which date the Interstate Commerce Commission prescribed a revised system (R. 345-456). That sys-

tem is still in effect and will remain so (Sec. 604 (a) of the Communications Act) until superseded by a valid order of the Federal Communications Commission.

The Communications Act of June 19, 1934, transferred to the Communications Commission the authority over telephone companies previously vested in the Interstate Commerce Commission, effective when the Communications Commission organized, which it did July 11, 1934. Prior to that date the Interstate Commerce Commission had been holding hearings on proposed changes in the system of accounts for telephone companies and filed a report (R. 15-84) on July 9, 1934, definitely condemning as unsound substantially the same proposal as was later adopted by the Communications Commission, that when a telephone company purchased property from any utility company "the original cost" to the predecessor company first dedicating the property to public use should be entered by the purchaser in its plant accounts and the balance of the amount paid should be placed in an "adjustment" account to be disposed of as the Commission might direct.* Following the transfer of authority to the Communications Commission it issued the order of June 19, 1935, here complained of.

The facts relating to the three requirements of the order which are assailed on this appeal are set forth below.

---

* The proposal rejected by the Interstate Commerce Commission differed from that adopted by the Federal Communications Commission in that it provided that the items in the adjustment account should be written off as "the commission having jurisdiction" might direct. The Interstate Commerce Commission said (R. 57) that "it may be remarked in passing" that this would involve an unauthorized delegation of power to state commissions, but it rejected the entire proposal for other reasons (R. 22, 28, 41, 43-46, 56-57).

Original Cost

Under the system now in effect all of a telephone company's investment in physical property is embraced in two balance sheet accounts, Account 100, "Telephone Plant", and Account 103, "Miscellaneous Physical Property" (R. 378-9). Account 100, "Telephone Plant", is subdivided into a series of accounts (the 200 series) known as telephone plant accounts, covering respectively, pole lines, cable, aerial wire, and other classes of plant. The telephone plant accounts also include account 278, "Undistributed Cost of Property", and Account 280, "Construction Work in Progress", and other items (R. 393). The sum of all the telephone plant accounts makes up the total of Account 100, "Telephone Plant".

The new system prescribed by the Communications Commission makes radical changes.

Account 103, "Miscellaneous Physical Property", is retained, but Account 100, "Telephone Plant", is abolished and three new balance sheet accounts are prescribed (R. 121) viz.,

100.1, Telephone Plant in Service
100.2, Telephone Plant Under Construction
100.3, Property Held for Future Telephone Use.

None of these accounts is to state the companies' own investment in the property, but instead must state the "original cost" of that property.

"Original cost" is defined as follows, Instruction 3-S. 1 (R. 101):

> "'Original cost' or 'cost', as applied to telephone plant, franchises, patent rights, and right-of-way, means the actual money cost of (or the current money value of any consideration other

than money exchanged for) property *at the time when it was first dedicated to the public use, whether by the accounting company or by a predecessor public utility.*" (Italics ours.)

The following instructions are also contained in the order:

"20. Purpose of telephone plant accounts. (A) The telephone plant accounts (201 to 277, inclusive) are designed to show the *original cost* (note Instruction 3-S. 1) of the company's telephone plant (note Instruction 3-BB), which ordinarily has a service life of more than one year * * * (R. 107). (Italics ours.)

"21. Telephone plant acquired. (A) When property in use in telephone service (note instructions 3-AA) is acquired, the amount of money actually paid (or the current money value of any consideration other than money exchanged) for the property (together with preliminary expenses incurred in connection with the acquisition) shall be charged to account 276, 'Telephone plant acquired'. (Note also account 139.)

"(B) The accounting for the acquisition of the plant shall then be completed as follows:

"(1) The original cost, estimated if not known, (note instruction 3-S. 1) of telephone plant, governmental franchises and other similar rights acquired shall be charged to the telephone plant accounts, account 100.2, 'Telephone plant under construction', and account 100.3, 'Property held for future telephone use', as appropriate, and credited to account 276. When the actual original cost cannot be determined and estimates are used, the company shall be prepared to furnish this

Commission with the particulars of such estimates.

* * * * * * * *

"(4) The amount remaining in account 276, 'Telephone Plant acquired', applicable to the plant acquired, shall upon completion of the entries provided in the foregoing paragraphs (1), (2), and (3), be debited or credited, as appropriate, to account 100.4, 'Telephone plant acquisition adjustment', except that when any amount thus chargeable to account 100.4 applies to duplicate or other telephone plant which will be retired by the vendee in the reconstruction of the acquired property and its consolidation with previously owned property, the accounting for the amount applicable to such plant shall be submitted to this Commission for consideration and approval. * * * (R. 108-109).

"100.1. Telephone plant in service. This account shall include the original cost (note instruction 3-S. 1) of the company's property used in telephone service at the date of the balance-sheet as classified under accounts 201 to 277, inclusive. (Note also instructions 3-AA, 20 and 21.) (R. 122.)

"100.2. Telephone plant under construction. (A) This account shall include the original cost (note instruction 3-S. 1) of construction of telephone plant not completed ready for service at the date of the balance-sheet. It shall include interest during construction, taxes during construction, and all other elements of cost of such construction work. (Note also instructions 20, 21, and 22.) * * * (R. 123.)

"100.3. Property held for future telephone use. (A) This account shall include the original

cost (note instruction 3-S. 1) of property owned and held for imminent use in telephone service under a definite plan for such use. * * * (R. 123.)

"100.4. Telephone plant acquisition adjustment. (A) This account shall include the difference between (a) the amount of money actually paid (or the current money value of any consideration other than money exchanged) for telephone plant acquired, plus preliminary expenses incurred in connection with the acquisition; and (b) the original cost (note instruction 3-S. 1) of such plant, governmental franchises and similar rights acquired, less the amounts of reserve requirements for depreciation and amortization of the property acquired, and amounts of contributions to the predecessor company or companies for construction and acquisition of such property. If the actual original cost is not known, the entries in this account shall be based upon an estimate of such cost. (Note also instruction 21.)

* * * * * * * *

"(C) The amounts recorded in this account with respect to each property acquisition shall be disposed of, written off, or provision shall be made for the amortization thereof in such manner as this Commission may direct. (Note also instruction 21.)" (R. 123-124.)

The net result of these rules is that when a telephone company has purchased physical property from another utility company, *the cost of that property to the company which first devoted it to public service, whether the vendor or a predecessor company,* is entered in Account 100.1, "Telephone Plant in Service", or Account 100.2, "Telephone Plant Under Construction", or Account 100.3, "Property Held for Future Telephone Use", as the case may be, and the differ-

ence between the "original cost" and what the accounting company paid for it, is to be entered in Account 100.4, the "adjustment" account, *to be disposed of or written off as the Commission may direct.* This requirement is not limited to sales between affiliates, but applies to all purchases.

The expert accountants who testified for the plaintiffs characterize this "adjustment" account as a mere suspense account, to be treated at all times as a deferred charge against surplus (R. 312, 320, 327-328, 338-339). Thus a part of the actual investment in property is removed from the property investment accounts on the balance sheet and placed in a suspense account which is characterized as something to be charged off, rather than as an investment. This is the situation even before any specific item is ordered to be written off. After any part of this account is written off a company's investment cannot be obtained by any combination of balances shown on the books.

There is no rule or principle prescribed for disposing of items in the "adjustment" account. There are no directions to accountants as to disposition of items therein. They are to be disposed of in accordance with the Commission's discretion in each particular instance, with no rule stated to guide it.

One further important fact remains respecting these property accounts. *The companies are forbidden to charge annual depreciation on any property in Account 100.4, "Telephone Plant Acquisition Adjustment."* (See Sections 220 (b) (g) of the Communications Act, Instruction 80 and paragraphs (A) and (C) of Instruction 81. R., 118-9. Instruction 82, R., 120.) By other provisions of the order, annual depreciation of physical property is to be charged in computing net annual operating income (R. 158), but property carried in Account 100.4 is excepted,

even while allowed to remain temporarily in that account, and of course, when written off as the Commission may immediately direct, the item disappears for good from the accounts. Omitting this depreciation from the annual statements of net operating revenue results in false and misleading statements to the public, stockholders and internal revenue agents. Thus the companies are not allowed to recover through depreciation charges their own investment in depreciable property, but must base their depreciation charges on the investment of some prior owner.

The requirements of the order are not limited to future transactions. The old accounts of the companies must be recast on the basis prescribed. Some of the plaintiffs have property, the prior ownership of which was scattered among hundreds of predecessor companies. This is commingled. The order requires that it be sorted out, tagged, and a different basis of accounting used, according to whether it was bought by the accounting company from a utility company or from a manufacturer (R. 335-336, 459, 462-467, 583).

Where actual cost to a predecessor utility is not known, its "estimated" cost is to be used.

The record shows beyond dispute that the expense of recasting the plant accounts on this "original cost" basis, will amount to several millions of dollars (R. 332, 340-341).

The Provision Respecting the Charging of Just and Reasonable Payments

Instruction 2(B.1) (R. 98) is as follows:

> "All charges to the accounts prescribed in this classification for telephone plant, income, operating revenues and operating expenses shall be

> just and reasonable and any payments by the Company in excess of such just and reasonable charges shall be included in account 323, 'Miscellaneous Income Charges'."

The statute makes it a penal offense to violate this instruction. (Communications Act of 1934, Sections 220 (d), 504, 220 (e), 220 (g), 501, 502.)

Every accounting entry for the purchase of property or for wages, salaries or any other expense, is to be made at the risk of prosecution.

Property Held For Future Use

The order of the Commission contains the following:

> "100.3 Property held for future telephone use. (A) This account shall include the original cost (note instruction 3-S.1) of *property owned and held for imminent use* in telephone service under a definite plan for such use" (R. 123). (Italics supplied.)

Thus, spare plant not being used in telephone service at the date of the balance sheet (Account 100.1, R. 122) and not under construction (Account 100.2, R. 123) must, if its use is not "imminent", be placed in Account 103, "Miscellaneous Physical Property" (R. 125).

The order does not permit taxes, maintenance charges or depreciation on "Miscellaneous Physical Property" to enter into computation of net operating income (Accounts 315 and 322, R. 162, Income Statement, R. 158, Items 7, 11 and 14). The word "imminent" is not defined. If given its ordinary meaning, "immediate", the result would be that spare plant provided in the exercise of good business judgment, to

supply service when needed, although not immediately for use, would be treated differently than plant in use and excluded from the operating accounts. If the word "imminent" is not given its ordinary meaning, it becomes so vague a term as to furnish no rule for accountants to act upon, and throws the whole subject into the field of decision by the Commission on the facts of each case.

Because of the nature of the telephone business, the same difficulty exists in determining whether certain portions of the spare plant are "used in telephone service at the date of the balance sheet," and so chargeable to Account 100.1, or are "held for imminent use" and chargeable to Account 100.3.

Specification of Errors

1. The District Court erred in refusing to enjoin the provisions of the Commission's order respecting "Original Cost," particularly in so far as it requires the difference between the amount paid for property by the accounting company and the cost to some prior owner to be entered in the adjustment account, to be charged off or disposed of as directed by the Commission, and to be excepted from charges for depreciation. Assignments of Error Nos. 1 to 9 and 23 to 31, inclusive (R. 587-593).

2. The District Court erred in refusing to enjoin the enforcement of Instruction 2(B.1) respecting just and reasonable outlay for property or expenses. Assignments of Error Nos. 10 to 14, inclusive, and 34 (R. 590, 593).

3. The District Court erred in refusing to enjoin the enforcement of the provisions for classification of physical property, including particularly the classifi-

cation based on "imminent" use, and the requirement that property not held for "imminent" future use should be placed in Account 103, Miscellaneous Physical Property (Assignments 14-18, R. 590-1).

4. The District Court erred in refusing to enjoin the enforcement of the whole order, on the ground that certain of the invalid provisions above mentioned and those it held void, are inseparable from the rest, and what remains is an incomplete and unworkable system of accounts. Assignments of Errors Nos. 20 to 22 inclusive and 35 (R. 591, 593).

Summary of Argument

I. The "original cost" provisions of the Commission's order are void. They are based on the fallacious theory that the cost of property to the public utility first devoting it to public use fixes its value for all purposes in the hands of succeeding owners.

They prevent telephone companies from recording their actual investment in their accounts, from recovering depreciation expense, which they actually incur, on their actual investment, and require them to base depreciation charges on the cost to a prior owner.

The discrimination in allowance of depreciation between property bought from a utility company and like property bought from others is wholly arbitrary.

The "original cost" provisions are unauthorized by statute. The difference between cost to the former owner and cost to the accounting company is to be disposed of in the discretion of the Commission. No rule or principle is prescribed for disposing of these items. The statute authorizes the Commission only to prescribe uniform rules. Here there is no rule

to guide a bookkeeper, or the action of the Commission. A direction by the Commission as to items in the Adjustment Account is not an interpretation of a rule. The provision in the statute authorizing the Commission to call for information on cost to former owners implies that the information shall be obtained from sources outside the accounts, not in them. The cost of recasting all accounts of property heretofore purchased from utilities would be enormous and an unreasonable burden.

The system prescribed by the Communications Commission has been rejected by the Interstate Commerce Commission, and held invalid by the courts of New York under a similar State statute.

II. The requirement in Instruction 2(B.1) that all charges for plant and operating expenses shall be "just and reasonable" and that all amounts paid for such purposes in excess of just and reasonable amounts shall be excluded from computation of net operating income and entered as "Miscellaneous Income Charges", is arbitrary and unauthorized by statute. It results in a false statement of net operating income, based on what the Commission may think should have been paid. It conceals the facts and actual operating expenses. The accounting company acts under peril of criminal prosecution if it enters what it has actually paid as a current operating expense. The penal provisions of the statute, coupled with the order, violate the Fifth Amendment, furnishing too vague a basis for criminal prosecution. The provision is obviously intended to enable the Commission to interfere in matters of management. The statute does not contemplate that the order prescribing accounts may be used as a

means or device to regulate the affairs of the telephone companies.

III. The classification of physical property is void. The requirement that under the account "Property Held for Future Telephone Use," may be placed only that held for imminent use is either arbitrary or void for indefiniteness.

If "imminent" means "immediate", the provision is void in excluding from computation of net operating income, maintenance, taxes and depreciation on property justifiably held for future but not immediate use. If the word "imminent" has not that connotation, then its meaning is too vague to form any guide to accountants and relegates decision on every item to the discretion of the Commission, and the provision is unauthorized by the statute, which contemplates a set of uniform rules, not individual directions by the Commission.

The dividing line between telephone plant in service and property held for future telephone use is likewise too vaguely defined to constitute a valid classification.

IV. The decisions of the courts are consistent with the appellants' contentions.

V. The system of accounts prescribed is incomplete and unworkable if the provisions complained of are stricken out, and the whole order should be enjoined, unless the Commission indicates its readiness to supply the defects before the new system is placed in effect.

Argument

I.

The "original cost" provisions are void.

That part of the Commission's order which requires property purchased from another utility to be carried in the companies' investment accounts at the amount it cost that former owner which first devoted it to public use, and which requires that the difference between that figure and the amount paid for it by the accounting company be placed in an adjustment account, to be disposed of, written off, or amortized as the Commission may direct, and which forbids an annual depreciation charge on that part of the purchase price in the adjustment account, obviously has its foundation in a theory that the cost to the predecessor company fixes the basis for rate making. No other explanation of these rules suggests itself.

Some authorities have striven for the rule that the prudent investment of the accounting company shall be adopted as the rate base. The theory that the cost to a former owner is to be used is one step farther away from anything recognized by decisions of the courts. To carry this theory to a logical conclusion, the Commission should have made a rule that the amount in the "adjustment" account should be immediately charged to surplus. In this respect the Commission lacked the courage of its convictions. Instead, it has attempted to avoid the issue by merely providing that amounts in the adjustment account shall be disposed of as the Commission may direct, without stating any principle on which it proposes to act. Its ultimate purpose may be carried out under

cover of this power. The effect of these provisions clearly tends to hamper the companies in maintaining records furnishing information for applying the established rules of rate making, but we do not contend that in this respect the order fixes a binding rate base. Notwithstanding the accounts are kept as required, it would be open to the companies in a rate case to disregard the plant accounts as recorded, and establish, if they can, the true rate base. This has been made clear in *Norfolk & Western Railway Co.* v. *United States,* 287 U. S. 134. Our attack upon the order is on different grounds. We contend:

1. The system prescribed is such as to prevent a company's investment accounts from showing its actual investment.

The original cost provisions require the plaintiffs' property investment accounts to be kept on a basis which will reflect neither the fact of their actual investment in their property nor its value, but which will conceal the actual investment and substitute, in the case of purchased property, the investment of a prior owner (estimated it not known). Sound accounting requires that a company's accounts shall show its own actual costs, and not the costs of some prior owner, or what some one thinks its costs should have been. The accountants who testified for the plaintiffs all agree that cost in accordance with established accounting practice is an individual matter. The records of an individual concern must show what its own costs are, never those of a competitor nor what its own costs might have been had other conditions prevailed or other decisions been made than those which were made. In other words, the record of each concern must provide an accurate his-

tory of what actually took place in that concern. Any other system is misleading and does not truly reflect the financial position (R. 309, 311, 319, 326).

The defendants contend that a company's plant investment may always be ascertained by adding together accounts

100.1, Telephone Plant in Service;
100.2, Telephone Plant Under Construction;
100.3, Property Held for Future Telephone Use; and
100.4, Telephone Plant Acquisition Adjustment.

If the Commission never exercises its power to order any item in Account 100.4 written off, this would be true, but the argument is not entirely frank. These items may be ordered written off immediately. Presumably they will be, sooner or later. It is no answer for the Commission to say the accounts will show total plant investment if the Commission does not exercise the powers it reserves. Furthermore, the "adjustment" account, 100.4, is merely a suspense account, with some further disposition in sight. The plaintiffs' accountants truly state that it is merely a deferred charge against surplus, that no careful accountant could fail to immediately treat it as such, and in all financial statements set up a reserve in equal amount. One says:

> "In truth, the balance shown under account 100.4 under the new system is a deferred charge, since the Commission may make it so at any time. Because of this uncertainty it is for all practical purposes an offset against surplus. A balance sheet which would fail to call specific attention on its face to the fact that the Commission *must* extinguish this item and may ex-

> tinguish it immediately by a write-off is incomplete and misleading, * * *" (R. 320).

What goes into the adjustment account is definitely removed from the investment accounts. The defendants will hardly contend that this order contemplates that the Commission will dispose of items in the adjustment account by transferring them to the investment accounts. The order specifically limits Accounts 100.1, 100.2 and 100.3 to the amounts of "original costs". There is no other property account to which they can be transferred. They stay where they are, or are written off. The fact, next referred to, that while in the adjustment account these items of cost of plant are not to be annually depreciated, confirms the fact that they are regarded as finally out of the investment column.

2. The "original cost" provisions are arbitrary because they prevent plaintiffs from recovering the depreciation expense which they actually incur.

It is undisputed that, under the order, charging depreciation on that portion of plaintiffs' investment which is included in Account 100.4 is forbidden, so that even if the Commission delays the write off for a longer or shorter period, and allows part of the cost of depreciable property to remain in that account, it may not be the basis of a depreciation charge.

In *Kansas City Southern Railway* v. *United States*, 231 U. S. 423, 448, the Court refers to depreciation as "an inevitable fact which no system of accounts can properly ignore."

The defendants contend that under the reserved power to amortize items in Account 100.4, it may, in its discretion, order them amortized by charges to

operating expenses. Here, again, they are not quite frank. Taking the order as a whole, it is obvious that there is no intention of treating anything but "original cost" as an investment or a basis for depreciation. Furthermore, the Commission should not have any discretion in the matter. If depreciation charges are to be based on cost there should be an absolute rule for using a company's own cost as the basis, and not the cost of another company. The system as it stands is illegal. It is no answer to say that the wrong may be corrected by a discretionary order in a particular case.

This system of accounts does have the effect of preventing plaintiffs from charging depreciation on part of their actual investment. A company is not allowed to recover, through depreciation charges, its own investment in property which is being used up, *but must base its depreciation charges on the investment of that former owner who first placed it in public service.*

Although in a rate case annual depreciation is based on value (*United Railways* v. *West,* 280 U. S. 234), it is not possible as a matter of current bookkeeping to make entries on that basis, as "value" may shift from time to time, and the universal practice is to use cost to the accounting company as a basis (see notes 23, 24 and 25, 280 U. S., pp. 266-270). In *Telephone and Railroad Depreciation Charges,* 177 I. C. C. 351, the Commission said at page 381:

> "It is not essential that the accounts should correspond in all respects with the facts which may be controlling in a confiscation case. In such a case the fact with respect to property, which is ascertained is its fair value, but we know of no system of accounts which undertakes to dis-

close this fact with respect to physical property. On the contrary, such property is normally stated in the investment account at cost. In determining whether confiscation has been or will be accomplished, the court will make allowance for unnecessary or unjustifiable operating expenses, but all such expenditures must be shown in the accounts. Accounting is not an exact science but a practical art which has evolved through a gradual process of trial and error and the application of sound judgment to experience."

The Commission also said at page 374:

"The practice which we have followed of basing depreciation charges upon original cost to the accounting company is general in this country."

The denial of the right to charge depreciation on that part of the cost in Account 100.4, is arbitrary for another reason. The property is classified for the purpose of fixing depreciation charges, not according to its character, or susceptibility to depreciation, but according to whether it was or was not bought from another utility company. If a telephone company buys poles from a timber company and builds a pole line, annual depreciation will be charged on the cost. If another line of poles, precisely like the first, is bought from an electric light company, the basis of depreciation charges is not the price paid, but the cost to a former owner. If a telephone company buys a building from a real estate company depreciation is charged on the price paid, but if it buys an identical building from another telephone company the depreciation base is that company's (or its predecessor's) cost. So with all classes of depreciable property.

3. The rules require a false and misleading statement of net operating income.

The result of these depreciation provisions is to falsify the income statement (R. 158-159). The system requires that allowed depreciation charges on physical property enter into the computation of net operating income, income available for fixed charges and surplus. By denying depreciation on part of the cost of depreciable property, the system falsifies the annual statements and requires the companies to make misleading statements in all these respects.

A fundamental objection to this system is that it has an eye only for a new theory as to a rate base and requires the companies to keep their accounts on that basis. It requires a company to keep its books on a basis which ignores its own actual transactions and falsifies its financial condition.

It ignores the fact that the accounts are not only for use in rate making, but for the information of the management, the shareholders, the investing public and the income tax collector. Accounts kept as this order prescribes would mislead all of those interested in what the operations of the companies actually are.

4. The original cost provisions are unauthorized by the statute in that they fail to prescribe any rule for the disposition of items in Account 100.4, but leave each individual accounting entry to the unfettered discretion of the Commission.

This objection, not the least formidable among those presented, is directed at that provision relating to disposing of items in Account 100.4. Under the head of "Telephone Plant Acquisition Adjustment" we find the following:

"The amounts recorded in this account with

> respect to each property acquisition shall be disposed of, written off, or provision shall be made for the amortization thereof in such manner as this Commission may direct" (R. 124).

Account 100.4, as we have shown and this rule plainly discloses, is a mere suspense account, in which part of the cost of property is to be placed to remain only temporarily before being carried to its final resting place.

No rule is laid down to govern the disposition of these items. The accountant's hand is stayed until the Commission acts in respect of each item. The statute gives no authority for such a method. It provides that:

> "The Commission may, in its discretion, *prescribe the forms* of any and all accounts, records and memoranda to be kept by carriers subject to this Act, including the accounts, records and memoranda of the movement of traffic as well as of the receipts and expenditures of moneys." (Italics supplied.)

In *Kansas City Southern Ry.* v. *United States,* 231 U. S. 423, the railroad urged that the Commission had power to prescribe the forms but not the substance. This Court rejected the distinction, saying, at page 443, that

> "* * * since, * * * uniformity in accounting is dependent upon the adoption and enforcement of *precise classification,* the authority to define the terms of the classification necessarily follows." (Italics ours.)

The Communications Act of 1934 authorizes a departure from uniformity only to the extent that the

Commission may classify carriers subject to this Act and prescribe different requirements under this section for different classes of carriers (Section 220 (h)).

The statute plainly requires the Commission to prescribe the forms of the accounts, not to reserve to itself the disposition of each particular item. It contemplates a system of accounts furnishing a complete guide to the accountant, a system of general rules, applicable alike to all telephone companies or all within a class. It falls short of attempting to delegate to the Commission the power to apply its discretion to the entry of particular items, in the absence of any rule. If the Commission in respect to any substantial part of a company's transactions may fail to prescribe such a rule and reserve the power to direct entries, in its discretion, then it may do so with respect to all entries, and the statute would be satisfied by an order merely providing that all entries shall be made as the Commission, in its discretion, may direct. Clearly this is beyond its authority.

The clause in the Communications Act, requiring six months' "notice of alterations by the Commission in the required manner or form of keeping accounts" is inconsistent with a grant of authority to establish no rule but to dictate individual entries in its discretion. The understanding the Interstate Commerce Commission had of its powers under a like statute is clearly shown in *St. Paul & Puget Sound Accounts*, 29 I. C. C. 508.

It has been suggested that the Interstate Commerce Commission has made a practice of issuing directions as to individual items. In a sense that is true, but a search of its reports confirms the assertion that in so doing, it was *merely interpreting and applying rules stated in its orders prescribing the forms of ac-*

counts. These interpretations have usually resulted from letters of inquiry from carriers or instances of apparent violation of regulations, and directions to make specific entries in accordance with these interpretations have usually been contained in letters or reports, as distinguished from orders. If such a direction is made and disobeyed, the prosecution would be for violation of the general regulation, not of the direction in the letter or report.

In the few cases where the Interstate Commerce Commission has by order directed a specific entry, the order has either been for the enforcement of a condition as to accounting which the Commission had previously attached to an order authorizing a carrier to acquire a property or issue securities, or has been in furtherance of existing general regulations as construed by the Commission. A number of these orders have resulted from fact finding which brought a transaction within the scope of an existing regulation.

See:

St. Paul & Puget Sound Accounts, 29 I. C. C. 508;

Reorganization & Control of Atlanta, Birmingham & Atlantic Ry., 117 I. C. C. 181; s. c. 117 I. C. C. 439; s. c. 158 I. C. C. 6;

Atlanta, Birmingham & Coast R. R. Co. v. *U. S.,* 28 F. (2d) 885; 37 F. (2d) 401; 282 U. S. 522; 201 I. C. C. 645; 12 F. Supp. 782; 296 U. S. 33;

Chesapeake & Ohio Case, 153 I. C. C. 9; 190 I. C. C. 382; 5 F. Supp. 7;

Norfolk & Western Case, 171 I. C. C. 557; 52 F. (2d) 967;

Norfolk & Western Ry. v. *U. S.,* 287 U. S. 134;

Saratoga & Encampment Valley Case, 192 I. C. C. 719;
New York Telephone Case, 188 I. C. C. 83;
Acquisition of Line by Jacksonville, Gainesville & Gulf Ry., 124 I. C. C. 623;
Acquisition of Line by Southern Pac. Co., 131 I. C. C. 726;
Control of Sewell Valley R. R. Co., 138 I. C. C. 85;
Acquisition of Lines by Gulf, Mobile & Northern, 154 I. C. C. 479;
C., M., St. P. & Pacific R. R. Co. Acquisition, 158 I. C. C. 770;
Rock Island System Consolidation, 193 I. C. C. 395;
Texas Midland R. R., 75 I. C. C. 1, 43.

Furthermore, there was no provision in the Interstate Commerce Act, as there is in the Communications Act, that six months' notice must be given of changes in the form of accounts. If a rule of the Interstate Commerce Commission was vague, a ruling by the Interstate Commerce Commission in a particular case could have the effect of an order prescribing a new rule.

5. The provision of the Communications Act authorizing the Commission to ask for information about cost to prior owners, supports our contention:

In the Court below, defendants relied on Section 213(c) of the Communications Act authorizing the Commission to require any carrier to file with the Commission a statement of "original cost at the time of dedication to the public use" of all or any part of the property of the carrier. This is found in the

section of the Act having to do with valuations and is one of the provisions in aid of valuations.

Their argument was that since the Commission could call for a statement of the information, it could require the companies' investment accounts to be carried on that basis. We draw the opposite inference. If the Congress had intended that the accounts might be kept on that basis it would have said so. The fact the information authorized to be requested is in the form of a separate statement, implies that it is to be collected from other available sources than the companies' current accounts. This conclusion is confirmed by Section 219(a) of the Act which requires the annual report to show the "cost" of the carrier's property. This cost must be derived from the accounts, and is obviously the cost to the accounting company.

6. Account 278 prescribed by the Interstate Commerce Commission is quite unlike the ones here assailed.

In the Court below, the defendants referred to Account 278 of the present system prescribed by the Interstate Commerce Commission as performing substantially the same function as Account 100.4 prescribed by the Communications Commission. There are great differences in principle and effect.

Account 278 of the present system represents the difference between the amount paid for property and its *structural value* (reproduction cost new less depreciation) at the time of purchase. It has nothing to do with cost to any prior owner. Where the amount paid for property is more than its structural value when bought, the excess is excluded from the depreciable property accounts and placed in Account

278, the theory being that if more is paid for property than the appraised value of its physical elements, the excess must have been paid for intangible elements, such as going value, which are not regarded as subject to depreciation (R. 45-46, 404).

Important differences between the treatment of Account 278 in the present system and Account 100.4 are as follows:

The present system permits the company to recover through depreciation charges the reproduction cost less depreciation existing at date of purchase, of purchased property. The system of the Communications Commission permits it to recover only what the property cost some former owner (less depreciation existing at date of purchase).

The present system does not subject Account 278 to being disposed of, written off or amortized at the will of the Commission. The company is permitted to write it off or amortize it but is not required to.

There is nothing in the present system which characterizes this account as a worthless or dubious asset. On the contrary, the balance in Account 278 is a part of the amount appearing in Account 100 as the company's total investment in telephone plant.

7. The cost of recasting the accounts on the basis prescribed is unreasonably burdensome.

The order requires recasting the accounts for all past transactions. The amount of property purchased by plaintiffs from other utilities is large. Since 1915 the plaintiffs have so purchased approximately $750,000,000 of property, involving well over one hundred thousand transactions. This property is commingled with other property not acquired from utility companies. Countless items of both kinds have been

retired, and identification would require search of detailed records of nearly the entire volume of purchased property, including that retired as well as that in existence (R. 335-6, 340-1).

Similar situations exist in respect of the additional and intervening plaintiffs.

The cost of this work would be several million dollars (R. 341).

The defendants answer that this expense may be imposed by the Commission under Section 213 (c). But the information as to actual (or estimated) cost to prior owners when obtained is of such doubtful value, even in a rate case as bearing on present worth of property, as to justify doubt as to whether the complete information required to recast the accounts could or would be asked for.

8. The system prescribed by the Commission has been rejected by the Interstate Commerce Commission as unsound, and by the New York courts as unauthorized by a state statute like the Communications Act of 1934.

The proposal to require costs to some prior owner to be set up in the plant accounts and the difference between that and the price paid by the accounting company to be placed in a suspense account to be dealt with by the Commission, was the subject of extended hearings by the Interstate Commerce Commission. On July 9, 1934, it filed its report rejecting the proposal as unsound (R. 22, 28, 41, 43-46, 56-57).

In the Court below the defendants pointed out (R. 543) and relied upon the fact that the Interstate Commerce Commission's definition of "original cost" was practically the same as that of the defendant Commission. It is true that in its report in the proceedings for a modification of the "First Revised

Issue", the Interstate Commerce Commission adopted a definition of original cost similar to the one involved in this case (R. 41). But the report provided that the term as thus defined be used only in the accounting for cost of franchises, and it left the accounting for telephone plant and other property on exactly the same basis as before. As franchises had always been accounted for on this basis, the adoption of this definition in the Interstate Commerce Commission's report had no effect whatever upon the accounting. Plaintiffs do not object to this as a definition, provided it is not used in prescribing the basis upon which they shall keep their property accounts. The Interstate Commerce Commission rejected the proposal that they be required to keep their property accounts on the basis of original cost as thus defined.

Public Service Law of New York, §66, subd. 4 grants to the Public Service Commission power to prescribe uniform methods of keeping accounts. The system prescribed by the Commission contained provisions defining and dealing with "original cost", like those in the order of the Communications Commission. Definition 31 defined "original cost" as the cost when first dedicated to public use. Account 143 was entitled "Suspense to be Amortized". In it was required to be placed any excess cost to the accounting company over the amount the property cost the first public utility owner. The disposal of items in this suspense account was covered by an instruction that they "shall be written off over such period and in such manner as the Commission by order may prescribe." The Appellate Division (*New York Edison Co. et al.* v. *Maltbie,* 244 App. Div. 685, 281 N. Y. S. 223), held these provisions void, as outside the authority granted by the statute: that the statute did

not vest in the Commission power to order a corporation to write off its books a loss it has not sustained; that actual cost is a relevant fact and that a corporation may not be compelled to make entries to conceal a relevant fact. The Court also said:

> "The petitioners argue, and with high judicial authority, that the books of a utility corporation are not kept solely for the information or benefit of the Commission; that stockholders, bond owners, the investing public and rate payers are interested; also that corporate financing is done upon the basis of book values."

The Court of Appeals of New York affirmed this decision. *Matter of New York Edison Co.* v. *Maltbie,* 271 N. Y. 103.

II.

The provision respecting the charging of just and reasonable payments is void.

This is contained in Instruction 2(B.1) (R. 98) which is as follows:

> "All charges to the accounts prescribed in this classification for telephone plant, income, operating revenues and operating expenses shall be just and reasonable and any payments by the Company in excess of such just and reasonable charges shall be included in account 323, 'Miscellaneous Income Charges'."

This requirement is arbitrary and unauthorized by the statute. It requires the accounts to record what in someone's judgment should have been spent rather than what was spent. The excess must be charged

to Account 323, "Miscellaneous Income Charges", and excluded from the computation of net operating income (R. 158, Items 7 and 15).

Net operating income is one of the most vital items in the companies' statements, of wide interest to investors and others. Whether an outlay of an operating expense was reasonable or unreasonable, being paid and non-recoverable, it nevertheless is an outlay which should enter into the computation of net operating income, and any system of accounts which forces a false statement of net operating income and conceals the truth as to the actual operating expenses, is arbitrary.

The statute, it will be remembered, makes it a penal offense for any company to fail to comply with the order prescribing the form of accounts. The accounting company acts at the peril of criminal prosecution in recording every item of outlay for property, wages, salaries, or other expenses. There may be the widest difference of opinion as to what is just and reasonable, but a company will hardly pay more for property or services than it believes they are worth. Presumably no part of any outlay would be treated by it, in the first instance, as unreasonable and charged to Account 323. It is then subject to prosecution, if the public authorities have a different opinion as to the reasonableness of the outlay. Of course, these provisions have the effect of denying due process under the Fifth Amendment, because there is an exaction of obedience to a rule so vague and indefinite as to be no standard at all.

United States v. *Cohen Grocery Co.*, 255 U. S. 81;

Tedrow v. *Lewis & Son Co.*, 255 U. S. 98;

Small Co. v. *American Sugar Refining Co.*, 267 U. S. 233;

Connally v. *General Construction Co.*, 269 U. S. 385;
Cline v. *Frink Dairy Co.*, 274 U. S. 445.

In the cases cited, both the penal provisions and the vague standard were contained in the statute. Here the penal provisions are in the statute and the vague and indefinite standard is in the order of the Commission. If this affords any basis for distinction, the answer is that the statute contemplates that the order prescribing the system of accounting shall be sufficiently definite that violations of it may be punished criminally, and any provision of the order for accounts which is so vague that violation of it may not be prosecuted is not authorized by the statute.

In a recent case before the Wisconsin Public Service Commission* an identical provision was assailed and stricken out by the Commission.

The obvious purpose of the provision is to allow the Commission, through fear of criminal prosecution, to impose its judgment on the company as to the reasonableness of every outlay. The statute authorizing the Commission to prescribe the form of accounts, gives no power to interfere in management, or require recording what the Commission may think should have been done, instead of what actually occurred.** There is nothing in the statute or the order which provides for any hearings or decision by the Commission as to the reasonableness of outlay. If, as defendants suggest, its advice should be sought,

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* In the *Matter of Prescribing a Uniform System of Accounts for Class A and Class B Telephone Utilities*, 2-U-902, decided December 20, 1935.

** See *New York Edison Co.* v. *Maltbie*, 244 App. Div. 685; 281 N. Y. S. 223 at page 226; also *People ex rel. New York Ry. Co.* v. *Public Service Commission*, 223 N. Y. 373, at page 378.

and not followed, the prosecution would be for violation of the original order prescribing the form of accounts. That provision is a plain usurpation of the right of management.

III.

The classification of physical property is void.

An important part of the property of all the companies consists of spare telephone plant, provided to meet additional demands for service in the most economical manner.

Under the Interstate Commerce Commission's system (now in effect) this property, as well as the telephone plant in use, is included in Account 100, Telephone Plant,* and the expense of its maintenance, depreciation, insurance and taxes is included in operating expenses and operating taxes and is considered in computing net operating income. Account 100, Telephone Plant, is one of the two main accounts into which the entire physical property is divided by the system now in effect. The other is Account 103, Miscellaneous Physical Property. The latter includes property "not held incident to the company's telephone operations", such as electric light plants or manufacturing plants, and also includes land, with the buildings and improvements thereon, which the company has acquired and is holding without any definite plan for use in telephone service or which has been retired

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* The words are "property used or held under a definite plan for telephone service" (R. 378). Of course all spare plant is held under a definite plan for use in telephone service when needed. Property such as land purchased for an indefinite possible future use, or property which has been finally retired from service, so as to be excluded from Account 100, is not considered spare plant.

from telephone service (R. 379, 59). What the Interstate Commerce Commission's system really does is to divide the property into two classes, telephone property and non-telephone property. It then provides that all expenses and taxes incurred in connection with the property in Account 103, "Miscellaneous Physical property," as well as the income therefrom, shall be excluded from the computation of net operating income.* This is, of course, entirely proper, since the property in this account, under the present system, is not held incident to the company's telephone operations.

The new system, like the existing one, provides that maintenance, depreciation, insurance and taxes on "Miscellaneous Physical Property" shall be ignored in arriving at net operating income.** But it differs radically from the existing system in that it classifies as "Miscellaneous Physical Property" all of the spare telephone plant which the companies are holding incident to their telephone operations, unless its use is "imminent". The new system divides the property into four accounts. These are:

100.1—Telephone Plant in Service. This includes the company's property "used in telephone service at the date of the balance-sheet" (R. 122).

100.2—Telephone Plant Under Construction. This includes plant "not completed ready for service" (R. 123).

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* See Accounts 315 and 322 of the present system (R. 409-410) and items 2, 6, 7, 11 and 14 of the Income Statement (R. 406).

** See Accounts 315 and 322 (R. 162) and lines 2, 6, 7, 11 and 14 of the Income Statement (R. 158).

100.3—Property Held for Future Telephone Use. This includes property "held for imminent use in telephone service" under a definite plan for such use (R. 123).

103—Miscellaneous Physical Property. This includes the company's physical property other than that included in the other three accounts, *i. e.*, it includes telephone property held for future use (under a definite plan or otherwise) if the future use is not imminent, as well as all non-telephone property (R. 125).

Thus plant which is not being "used in telephone service" and is not under construction, must go into either Account 100.3, "Property Held for Future Telephone Use" or into Account 103, "Miscellaneous Physical Property"—into the former if its use is "imminent", otherwise into the latter. The dividing line between these two accounts depends on the construction of the word "imminent".

What is meant by the word "imminent"?

According to the dictionaries and the courts, an event is imminent if it "threatens to occur immediately", is "near at hand", or "on the point of beginning". *Webster's International Dictionary; The Queen of the Pacific,* 25 Fed. 610; *Eckhardt* v. *City of Buffalo,* 19 App. Div. 1; *State* v. *Gateway Mortuaries,* 87 Mont. 225; *Smith* v. *City Ice & Delivery Co.,* 117 Kan. 485; *Julius Kessler & Co.* v. *Southern Ry. Co.,* 200 Ky. 713; *Pierce* v. *C. H. Bidwell Thresher Co.,* 158 Mich. 356.

The Commission can hardly have used the word in that sense. If it did, items in Account 100.3, Property Held for Future Telephone Use, would have to be transferred to Account 100.1, Telephone Plant in Service, almost before the ink dried on the first entry,

and property held for future telephone use would have to be placed in Account 103, Miscellaneous Physical Property, if not intended for immediate use, although necessarily provided for use in the future, in the performance of the duty to be ready to supply service, and while in Account 103 no costs of its maintenance, taxes or depreciation could be considered in computing net operating income. Such a requirement would obviously be arbitrary and grossly unreasonable.

If "imminent" does not mean "immediate" or "on the point of beginning", what is its meaning?

There will then be the widest difference of opinion as to whether the use of property is imminent. The word is too vague to define an accounting classification. All of the accounting experts for the plaintiffs so characterize it (R. 314-315, 322-323, 329, 341), and the experts for the defendants attempt no defense or explanation.* A rule depending on the construction of this word is so vague as to be no rule at all.

There is no reason why these important classifications cannot be made reasonably definite. It appears that instead of doing this the Commission has purposely made these classifications vague and has made the requirement, which defendants vigorously stress in this connection (R. 295, 491), that doubtful cases shall be submitted to it "for consideration and decision" (R. 104). Where the classifications are so vague that most cases are doubtful this will amount, in practical effect, to the dictation of individual accounting entries in the Commission's discretion. It

* The Interstate Commerce Commission rejected the proposal of certain state commissions to place telephone plant in the Miscellaneous Physical Property account unless there was a definite plan for its use "within one year" (R. 42, 69). The words "within one year" are less vague than "imminent", although both are based on *predictions* rather than upon factual situations.

is identical in principle with the Commission's proposal to determine whether an expenditure is just and reasonable by an "interpretation" in each individual case. It amounts to the same thing as the requirement that the items in the Telephone Plant Acquisition Adjustment account shall be written off as the Commission may direct in each instance. There the Commission explicitly undertakes to dictate individual accounting entries in the absence of rules, while here and in the case of the "just and reasonable payments" it proposes to do the same thing under guise of interpreting rules so vague as to be no rules at all.

The Commission is without authority to direct accounting entries in this manner. Its authority is to prescribe rules applicable alike to all carriers or to all within a class (Section 220 h). This court has said that one of the prime purposes of prescribed accounting for carriers is uniformity (*Norfolk and Western Ry. Co.* v. *United States,* 287 U. S. 134, 140) and that "uniformity in accounting is dependent upon the adoption and enforcement of precise classification" (*Kansas City Southern Ry. Co.* v. *United States,* 231 U. S. 423, 443). There has been no attempt at precise classification here. We concede that complete precision is not always attainable and that any classification may require interpretation when unusual or unforeseen cases arise, but this is no excuse for making the classification so vague and undefinable that a separate fiat may be made in each case under guise of an "interpretation" applicable to the facts of that case. This is the antithesis of uniformity.

The meaning of the word "imminent", when applied as here to property held for *future* use, is so

uncertain that almost any entry made by a company's accountants could be challenged by the Commission. The Commission would then settle the entry by an "interpretation". By its "interpretation" (*e. g.*, by saying that the use of a particular cable or section of switchboard is imminent or the reverse) the Commission will say that the vague accounting rule requires the entry in question to be made in a particular way. The company must then follow this advice or risk prosecution, but the prosecution would be for violation of the original vague rule. If punishment under this vague rule were valid the Commission could thus compel the company, through fear of penalties, to make individual accounting entries in accordance with the Commission's discretion in each instance. But if punishment would be invalid, on the ground that exaction of obedience to a standard so vague is a denial of due process,* then the accounting rule is clearly invalid.

We can perceive no purpose to be served by this accounting scheme unless it is regarded as an attempt to pre-judge the issue of used and useful property in rate cases, or as a means of enabling the Commission to substitute its judgment for that of the management as to how much spare plant shall be provided for fluctuations in traffic and for growth, compulsion being exercised by compelling the companies to ignore, in computing net operating income, any spare plant in excess of that deemed desirable by the Commission. These are not proper functions of an accounting system.

The system is likewise vague as to the property to be included in Account 100.1, Telephone Plant in Service. This is to embrace property "used in tele-

* See cases cited on pages 37-8 of this brief.

phone service at the date of the balance sheet". Superficially this appears to be definite, but because of the nature of telephone plant and the conditions of its use it is too vague to constitute a workable basis for differentiating between this account, and Account 100.3 and Account 103. Much of the property of every telephone company consists of large units which are made up of smaller units. For example, switchboards consist of large sections, some of which often are unused. Is the entire switchboard "used in telephone service," and thus to be charged to Account 100.1, or are the unused sections to be considered as held for future use and charged to Account 100.3 or Account 103, depending on whether the future use is imminent? An underground conduit consists of a number of ducts, only a part of which initially contains cables; the cables themselves consist of many pairs of fine wires, some of which are spares; buildings initially contain vacant floor space. There is the same question as to each. Experience in rate cases has shown it to be a controversial one. The system of accounts leaves it unanswered (R. 342, 314, 322, 329, 333). It would be easy to answer. *While the system was in tentative form plaintiffs specifically asked the Commission to answer this question and incorporate the answer in the system, but their request was ignored* (R. 555-557).

In this litigation the Commission's witnesses have given their interpretation of the words "used in telephone service" as applied to spare plant. Thus the witness Colbert says that where any wires in a cable are in use the entire cable is "used" and should be charged to Account 100.1, Telephone Plant in Service, and we understand him to mean that the same is true of spare plant generally, such as idle

sections of switchboards, vacant ducts in conduits and vacant floor space in buildings (R. 528-9, 530). However, other witnesses for the Commission take a different view. Its chief accountant, Norfleet, says that only "necessary" spare plant is to be included in Account 100.1 (R. 481). His idea apparently is that the Commission will decide how much spare plant is necessary in each case. Its accountant, Rains, indicates that the companies should not attempt to interpret these classifications themselves and suggests no interpretation of his own. He apparently realizes the patent uncertainty and thinks the companies should ask the Commission what to do whenever in doubt as to an entry. He thus admits there is no rule to guide accountants (R. 491). If the Commission would change its system of accounts to conform to the interpretation of the witness Colbert, as we have stated it, appellants would be satisfied on this point.* This would not, however affect the ambiguous dividing line between Accounts 100.3 and 103, resulting from use of the word "imminent," as to which all of defendants' witnesses are silent.

The Wisconsin Commission, when these identical provisions were attacked in a proceeding before it, disposed of the entire question of the classification of physical property in a manner which was acceptable to the companies and should satisfy every legitimate need of regulation. That Commission determined that Account 100.1 should include spare

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* While the system of accounts was still in tentative form, plaintiffs formally requested, in writing, that it be changed to conform to this interpretation, but this request was refused (R. 555-556).

plant such as unused circuits in a cable, as well as plant temporarily out of service. It said:

> "It appears that this matter is dependent upon the interpretation of the word 'used' in the text of account 100.1, Telephone Plant in Service. This account includes the original cost of the company's plant used in telephone service. The term 'used' should be interpreted broadly. For accounting purposes, plant will be considered as used even though it is not giving service to the full extent of its capacity. The cost of a cable, for example, should be included in account 100.1, even though some of the circuits are not rendering service. This means that for accounting purposes, spare plant, that is, plant that is used, though not to its full capacity, is includable in account 100.1, Telephone Plant in Service. We also interpret the term 'used' in account 100.1 as including, for accounting purposes, plant which is temporarily out of service."

Such a clarification of Account 100.1 would satisfy appellants, but we have no assurance it will be so interpreted, because, though requested (R. 555-6), the Communications Commission has refused to modify or clarify the definition.

The Wisconsin Commission also modified the definition of Account 100.3 to read as follows:

> "This account shall include the original cost (note instruction 3 S.1) of property owned and held for future telephone use."

It struck out the word "imminent".

Under the system thus construed and amended all plant which is used, including its spare capacity, goes into Account 100.1, Telephone Plant in Service;

all plant which is held for future telephone use goes into Account 100.3, Property Held for Future Telephone Use, regardless of the imminence of its use; and Account 103, Miscellaneous Physical Property, includes only non-telephone property.

IV.

The decisions of this Court are consistent in every respect with appellants' contentions.

The decisions of this Court have been well summarized in *Chesapeake and Ohio Ry. Co.* v. *United States,* 5 F. Supp, 7, 10, where the Court said:

> "* * * The order complained of requires the carrier to keep its accounts in a particular manner, and, in effect, if its contention is sound, denies it the right to maintain its equipment out of earnings, requires it artificially to inflate and enlarge its investment and decrease its income accounts, and keep its books upon an unreal and untrue basis. The only ground upon which it can be said that the carrier suffers no legal injury as a result of an order having such effect, is that mere accounting entries are involved and that, in the absence of immediate pecuniary or other damage, no legal injury can result. The law, however, is otherwise. The decisions recognize that the right to maintain a reasonable system of accounting is in itself a legal right the deprivation of which will entitle a carrier to relief, if it can show that the order complained of exceeds the commission's authority or is wholly arbitrary or unreasonable. See *I. C. C.* v. *Goodrich Transit Co.,* 224 U. S. 194, 32 S. C. R. 436, 56 L. Ed. 729; *Kansas City So. Ry. Co.* v. *U. S.,* 231

U. S. 423, 440; 34 S. C. R. 125, 58 L. Ed. 296, 52 L. R. A. (N. S.) 1; also opinion below (Com. Ct.), 204 F. 641, 644; *Norfolk & Western Ry. Co.* v. *U. S.*, 287 U. S. 134, 143, 53 S. C. R. 52, 77 L. Ed. 218. In these cases the courts took jurisdiction and reviewed on their merits orders requiring a particular method of accounting."

In the *Norfolk & Western* case (287 U. S. 134, 138), the rules of the Interstate Commerce Commission required railroad companies to divide their assets into two general classes: namely, investment in road and equipment and miscellaneous or non-transportation property. The Norfolk & Western Railroad owned certain coal lands which it alleged were used exclusively for supplying coal as fuel for its locomotives. It insisted that those lands constituted an item of investment in road and equipment. The Commission held to the contrary and ordered that the property be included among the miscellaneous or non-transportation property.

The Court pointed out that few if any other railroads were situated like the Norfolk & Western with respect to its coal lands (p. 141); that uniformity of reporting for the purpose of comparing results would require that the Norfolk & Western keep its books in manner similar to those kept by the other railroads (pp. 140-141); and that the amount of return to which the company was entitled under the recapture provisions of the Transportation Act would not be affected because it would be given an opportunity in a recapture proceeding to present any claims with regard to the inclusion of the property (p. 141). Certainly in this case the railroad company failed completely to show that the order of the Commission was unreasonable, arbitrary or contrary to sound accounting principles.

In the *Kansas City Southern* case (231 U. S. 423) the railroad company built originally a road with heavy grades appropriate for the light traffic and trains of that period. Under the demands of heavier traffic it eliminated the heavier grades at some points by laying new sections of track at other points and abandoned the roadbed first constructed. It sought to include in its capital accounts the total amount spent for both the new tracks and roadbed and the abandoned roadbed and to ignore the fact that a substantial amount of mileage had been abandoned. The order of the Commission required that the cost of the abandoned track and roadbed be deducted from and that of the new track and roadbed be added to the capital accounts. So far from the order of the Interstate Commerce Commission concealing the facts or requiring improper accounting, that order required that all the facts be given effect to, the abandonment, as well as the new construction.

The court naturally and properly held that the order of the Commission was not unreasonable and not arbitrary.

Of course, when the new tracks were laid and the old roadbed abandoned, the railroad had nothing but the existing property. The abandoned roadbed had been retired from service.

The law is settled that the plaintiffs are entitled to relief, if the provisions complained of are outside the authority granted by the statute or are so arbitrary or unreasonable as to constitute an abuse of power. In the respects above stated we have shown these conditions exist.

Even a Chinese in the Philippines has a right to keep a truthful set of books, needed in his business to show his actual transactions.

Yu Cong Eng v. *Trinidad*, 271 U. S. 500.

V.

The provisions assailed are not severable and the whole order is void.

We believe that with the elimination of the provisions enjoined below and those assailed here,* the remainder of the accounting system is incomplete and unworkable. Large gaps appear in its structure. The eliminations leave many important matters unprovided for, with no rule to guide the accountants. The system is unworkable unless the gaps may be filled by the accountants by substituting provisions which in their opinion are consistent with sound accounting.

When we sought a stay pending this appeal this question was raised but left unsolved. The Justice of this Court who granted the stay applied it only to the provisions complained of, reserving in his order the right to consider a stay of the whole order if further application were to be made. Thereupon the Commission, apparently realizing that the gaps left in its system of accounts were serious, suspended the effective date of the whole of its Telephone Division Order No. 7-C, to await the decision of this Court. If our contentions are sustained, doubtless the Commission will consider it wise to fill the gaps with new provisions and fix a new effective date for the inauguration of the system in the manner prescribed by the statute. If it so declares its intention the Court will be relieved of the task of considering

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* This statement is not intended to embrace Instruction 2(B.1), respecting just and reasonable payments, nor the instructions as to contributions which were enjoined by the court below. We concede that these provisions are severable.

whether what is left of the system is separable and workable. If no such proposal is made by the Commission, we rest on our position that the system is incomplete without the provisions objected to.

Respectfully submitted,

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1936.

No. 74.

AMERICAN TELEPHONE AND TELEGRAPH COMPANY, *et al.*,

Appellants,

vs.

THE UNITED STATES OF AMERICA, FEDERAL COMMUNICATIONS COMMISSION and NATIONAL ASSOCIATION OF RAILROAD AND UTILITIES COMMISSIONERS,

Respondents.

MOTION BY APPELLANTS FOR LEAVE TO FILE MEMORANDUM IN RESPONSE TO THAT FILED BY THE FEDERAL COMMUNICATIONS COMMISSION.

Now come the appellants and ask leave of the Court to file the attached memorandum, commenting on the memorandum filed since the argument by the Federal Communications Commission.

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Respondents.

MEMORANDUM BY THE APPELLANTS COMMENTING ON THE MEMORANDUM FILED BY THE FEDERAL COMMUNICATIONS COMMISSION.

A study of the memorandum filed by the Federal Communications Commission results in the conclusion that it is a wholly unsatisfactory proposal in the following respects:

1. It is not merely th interpretation of an ambiguous provision of the order, but calls for special orders of the Commission in conflict with express provisions of the regulations.

It thus accomplishes in effect an amendment to the rules, and we believe that amendments should be effected as the law provides by order of the Commission and not by any proposal made by the Commission in court.

2. The proposal or pledge of the Commission as to what it proposes to do, being inconsistent with the scheme of the published order, will leave the whole matter of depreciation with respect to purchased property in the greatest confusion.

3. The proposal of the Commission still fails to prescribe any rule or standard either for accountants or to control or guide the action of the Commission.

We concede that in case of an ambiguous rule it is competent for the Commission to suggest an interpretation acceptable to the Court which would make the ambiguous rule as so interpreted satisfy the requirements of the law. The appellants suggested such a solution in respect of that part of the controversy covered by paragraph III of our brief, which arose because of an ambiguity as to whether spare plant should be classified by the accountants under the head of "Plant in Service" or "Plant Held for Future Use". We made that suggestion because our point about the rules affected was that they were ambiguous.

Quite a different situation is presented in connection with the proposal of the Commission pertaining to account 100.4. Our contention there is that the rules are not ambiguous, but as drawn they are arbitrary and not within the authority granted by the statute.

We have the following comments to make about the proposal:

(a) The rules as drawn make the so-called original cost to the first dedicator the basis for entries in the plant accounts and the basis for computing

depreciation on depreciable plant. This point was brought to the front by the question asked of the Attorney General by Mr. Justice Roberts. That question was, Supposing the price paid for property acquired from another utility company was less than the original cost, would the original cost, being more than the price paid, be left in plant accounts? The Attorney General answered that it would, but that the difference between the price paid and the original cost would be entered as a credit, not a debit, in the adjustment account. This answer was correct as far as it went, but it is obvious that the original cost, even though in excess of the price paid, thus remains in the plant accounts, constituting by the express terms of the order the basis for computation of depreciation on tangible property. This fact confirms our assertion that the fundamental theory of the system as promulgated makes the original cost, whether more or less than the price paid, the basis for depreciation accounting.

(b) The Commission proposes that it will grant under paragraph (C) of account 100.4 the equivalent of depreciation under the guise of amortization. When amounts paid by the accounting company have been finally determined "to be definitely attributable to depreciable telephone plant" the Commission says it will provide for their amortization through account 613 or account 675. Account 613 (R. 186) is for amortization of intangible property, and covers only "franchises, patents leaseholds and similar intangible property." None of these items is included in the "classes of depreciable telephone plant" which the Commission has prescribed (R. 120) pursuant to the mandate of Section 220(b) of the Act. To charge to this account the depreciation on amounts which have

been held to be "definitely attributable to depreciable telephone plant" would require an amendment of the system. Account 675, Other Expenses, covers only "operating expenses not properly chargeable to other accounts." Depreciation on amounts "definitely attributable to depreciable telephone plant" is necessarily properly chargeable to the depreciation account, and account 675 excludes it by its terms. Depreciation account 608 would not thus truly show at any time the depreciation allowed on tangible property and the depreciation reserve account 171 would not truly show at any time the full provision for depreciation on tangible depreciable property.

(c) Under the published order, part of the price paid for property purchased from other utilities would go into plant accounts and part into the adjustment account. The proposal of the Commission still takes no account of the fact that when property is retired it should be dropped out of both accounts and thus it would be necessary in the case of retirement of every item of property, any part of the cost of which was entered in the adjustment account, for the Commission to make a special order allowing retirement from the adjustment account simultaneously with retirement from the plant accounts.

The accounting for property retired is prescribed by Instruction 25 (R. 112-113) and provides that when an item is retired its original cost shall be written out of the plant accounts (the 200 series, which in total make up account 100.1). It makes no provision for writing out of account 100.4 the difference between the original cost and the actual cost of the item retired. It cannot be that by saying "provision will be made" the Commission means

that separate provision will be made in the case of each retirement. Individual poles, telephones and similar items are being retired every day and will soon run into the millions. Such items are indistinguishable as between those purchased from a predecessor utility and those initially provided by the accounting company (R. 340, 341). In the nature of the case, the only provision that can be made is to provide an accounting rule, applicable to all transactions of a specified kind, which the companies themselves can and will be required to apply in the keeping of their accounts. Such a rule has not been made, and if made would necessarily constitute an amendment to the system.

Moreover, under the system as it stands (even if paragraph (1) of the Government's memorandum should be regarded as a part of it) a company's total investment could not be ascertained from its accounting balances by adding accounts 100.1, 100.2, 100.3 and 100.4, after the first day, because thousands of items of property are being retired daily, and there is no provision for writing out of these accounts anything except their "original cost".

(d) The proposal makes no suggestion as to what standard the Commission would apply in determining whether under the circumstances of the particular case amounts in account 100.4 may be deemed to represent an investment in tangible property. The Commission in its argument seems to have rejected the system heretofore followed by the I. C. C. that there shall not be entered in the plant accounts any portion of the price paid in excess of the "structural value" of the tangible property acquired, and yet it does not indicate in its proposal what standard will be applied. It still has failed to prescribe any rule

or standard either to guide accountants or the action of the Commission.

(e) The record shows (R. 336) that the appellant companies in the Bell Telephone System have, during the last twenty years, made more than 100,000 purchases of property from other utilities. The proposal involves a separate determination with respect to each of these past transactions as well as all future purchases before the accountants can make any final disposition of them.

We do not feel justified in burdening the Court with a further analysis of the situation resulting from the Commission's proposal. We think it is too clear to be controverted that the published order makes the original cost, whether more or less than the price paid, the basis for entries in the plant account for plant investments and for computation of depreciation; that the provision for amortization as an intangible of an item in the adjustment account was never intended by these rules to be used as a substitute for depreciation of depreciable property; that account 675, the alternative suggested in the proposal, is plainly inapplicable; that the use of the amortization provision as a substitute for depreciation of tangibles, confuses the accounts, placing the resulting charges under accounts intended for amortization of intangibles; and that the proposal still leaves the Commission unbound by any rule or principle in dealing with items in account 100.4. We cannot escape the conclusion that the proposal which the Commission makes with respect to the use of the amortization as a substitute for depreciation allowances is in direct conflict both with the fundamental scheme relating to original cost and with specific provisions of the

rules, and that what the Commission proposes constitutes amendments unsatisfactory in themselves and not interpretations of ambiguities and that amendments should be made by Commission order and not by assurances or pledges made in court. The Commission should make rules on which the accountants may act. If the accountants misinterpret or misapply the rules it should then be open to the Commission to make orders interpreting and applying them, but the proposal to leave the rules silent as to the disposition of entries relating to important transactions with the power to the Commission to dictate the entries to be made, is not in conformity with the letter or spirit of the statute.

Respectfully submitted.

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In the Supreme Court of the United States

OCTOBER TERM, 1936

No. 74

AMERICAN TELEPHONE AND TELEGRAPH CO. ET AL., APPELLANTS

v.

THE UNITED STATES OF AMERICA, FEDERAL COMMUNICATIONS COMMISSION, AND NATIONAL ASSOCIATION OF RAILROAD AND UTILITIES COMMISSIONERS

ON APPEAL FROM THE DISTRICT COURT OF THE UNITED STATES FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF FOR THE UNITED STATES

OPINION BELOW

The opinion of the United States District Court for the Southern District of New York (R. 561) is reported in 14 F. Supp. 121.

JURISDICTION

The decree of the District Court was entered March 24, 1936. (R. 584.) Petition for appeal

was filed April 6, 1936, and was allowed the same day. (R. 586, 594.)

Jurisdiction of this Court is conferred by Sec. 402 (a) of the Act of June 19, 1934, c. 652, 48 Stat. 1093 (U. S. C., Title 47, Sec. 402 (a)), and by the Act of October 22, 1913, c. 32, 38 Stat. 220 (U. S. C., Title 28, Sec. 47), as amended by the Act of February 13, 1925, c. 229, 43 Stat. 938 (U. S. C., Title 28, Sec. 345).

QUESTIONS PRESENTED

The attack upon the "original cost" provisions of the order of the Federal Communications Commission concerns the accounting prescribed for property already in public service which is acquired from another public utility, whether a controlled or independent company, and which the acquiring company uses or is about to use in telephone service. The order of the Commission provides that, in the case of such acquisitions, the cost of the property to the company which first dedicated it to public service shall be included by the acquiring company in one set of balance-sheet accounts, and the difference between such "original cost" and the amount paid for the property by the accounting company (whether in cash or other consideration) shall be credited or debited to another balance-sheet account, account 100.4. These and other related provisions give rise to the following questions:

(1) Whether the segregation of amounts represented by account 100.4 into a separate balance-

sheet account is so arbitrary as to be unauthorized by the Act and in violation of the Fifth Amendment. There is also involved the subsidiary question whether account 100.4 is a suspense account or, as its classification indicates, a telephone plant investment account.

(2) Whether a provision by virtue of which the Commission may, when appropriate, direct that amounts in account 100.4 be written off is so unreasonable as to be unauthorized by the Act and in violation of the Fifth Amendment.

(3) Whether the provision that amounts in account 100.4, after they have been subdivided according to their character, shall be written off, amortized, or other disposition thereof made, as the Commission shall direct, is unauthorized by the Act because the provision in question does not itself set forth the rules to be applied by the Commission in issuing these directions.

(4) Whether the failure to allow depreciation as such against amounts in account 100.4, even though the Commission may, in appropriate circumstances, permit an equivalent operating-expense charge, is so arbitrary as to be unauthorized by the Act and in violation of the Fifth Amendment.

(5) Whether the cost and trouble involved in complying with the original cost provisions is so burdensome as to constitute a violation of the Fifth Amendment.

Apart from the foregoing questions arising under the original cost provisions, the following further questions are presented:

(6) Whether the requirement that the charges to certain accounts shall be just and reasonable and that payments in excess thereof shall not be included in operating expenses is so arbitrary as to be unauthorized by the Act and in violation of the Fifth Amendment.

(7) Whether certain classifications of physical property are so indefinite as to be unauthorized by the Act and in violation of the Fifth Amendment.

STATUTE INVOLVED

Section 220 of the Act of June 19, 1934, c. 652, 48 Stat. 1078 (U. S. C., Tit. 47, Sec. 220), known as the Communications Act of 1934, provides in part as follows:

> (a) The Commission may, in its discretion, prescribe the forms of any and all accounts, records, and memoranda to be kept by carriers subject to this Act, including the accounts, records, and memoranda of the movement of traffic, as well as of the receipts and expenditures of moneys.
>
> (b) The Commission shall, as soon as practicable, prescribe for such carriers the classes of property for which depreciation charges may be properly included under operating expenses, and the percentages of depreciation which shall be charged with respect to each of such classes of property,

classifying the carriers as it may deem proper for this purpose. The Commission may, when it deems necessary, modify the classes and percentages so prescribed. Such carriers shall not, after the Commission has prescribed the classes of property for which depreciation charges may be included, charge to operating expenses any depreciation charges on classes of property other than those prescribed by the Commission, or, after the Commission has prescribed percentages of depreciation, charge with respect to any class of property a percentage of depreciation other than that prescribed therefor by the Commission. No such carrier shall in any case include in any form under its operating or other expenses any depreciation or other charge or expenditure included elsewhere as a depreciation charge or otherwise under its operating or other expenses.

* * * * *

(d) In case of failure or refusal on the part of any such carrier to keep such accounts, records, and memoranda on the books and in the manner prescribed by the Commission, or to submit such accounts, records, memoranda, documents, papers, and correspondence as are kept to the inspection of the Commission or any of its authorized agents, such carrier shall forfeit to the United States the sum of $500 for each day of the continuance of each such offense.

(e) Any person who shall willfully make any false entry in the accounts of any book

of accounts or in any record or memoranda kept by any such carrier, or who shall willfully destroy, mutilate, alter, or by any other means or device falsify any such account, record, or memoranda, or who shall willfully neglect or fail to make full, true, and correct entries in such accounts, records, or memoranda of all facts and transactions appertaining to the business of the carrier, shall be deemed guilty of a misdemeanor, and shall be subject, upon conviction, to a fine of not less than $1,000 nor more than $5,000 or imprisonment for a term of not less than one year nor more than three years, or both such fine and imprisonment * * *.

* * * * *

(g) After the Commission has prescribed the forms and manner of keeping of accounts, records, and memoranda to be kept by any person as herein provided, it shall be unlawful for such person to keep any other accounts, records, or memoranda than those so prescribed or such as may be approved by the Commission or to keep the accounts in any other manner than that prescribed or approved by the Commission. Notice of alterations by the Commission in the required manner or form of keeping accounts shall be given to such persons by the Commission at least six months before the same are to take effect.

Other pertinent provisions of the Act are set forth in the Appendix, *infra,* pp. 71–74.

STATEMENT

This is an appeal from a decree of a specially constituted three-judge District Court dismissing, except in two minor particulars, a bill to set aside and enjoin an order of the Federal Communications Commission issued on June 19, 1935, to become effective on January 1, 1936, prescribing a uniform system of accounts for telephone companies subject to the Communications Act of 1934. The plaintiffs and intervening plaintiffs below are the American Telephone and Telegraph Company and 36 telephone companies controlled by it, which will sometimes be referred to herein as the Bell companies. (R. 2–3, 244–245, 335; Moody's 1935 Public Utilities Manual, pp. 82, 83, 94, 116.) The additional plaintiffs below are 7 telephone companies independent of the Bell system, but controlled by a single holding company, which group will sometimes be referred to as the Associated companies. (R. 237; Moody's 1936 Public Utilities Manual, pp. 2088–2089). All 44 plaintiffs have joined in the appeal. The facts and issues are the same as to both groups of appellants, except that the "original cost" provisions of the system of accounts prescribed by the Commission affect a very much larger proportion of the property of the Associated companies than of the Bell companies.

The present proceeding was instituted pursuant to Section 402 (a), *infra*, p. 73, of the Communications Act of 1934 (hereinafter sometimes referred

to as the Communications Act). This section provides that the statutory provisions relating to the enforcement or setting aside of orders of the Interstate Commerce Commission shall apply to suits to set aside orders of the Communications Commission (with exceptions immaterial here). Appellee, National Association of Railroad and Utilities Commissioners, representing the regulatory commissions of 46 states, which had taken part in the proceedings before the Communications Commission leading to the order under attack here, was allowed by the District Court to intervene as a party defendant in support of the Commission's order. (R. 266, 268, 271.)

Prior to the enactment of the Communications Act, the accounts of telephone companies engaged as common carriers in interstate communication were subject to regulation by the Interstate Commerce Commission under Section 20 (5) of the Interstate Commerce Act.[1] Section 220 of the Communications Act, which closely parallels the language of various subsections of Section 20 of the Interstate Commerce Act, conferred upon the Communications Commission authority to prescribe the accounts to be kept by such telephone carriers. The Communications Act repealed the

[1] This authority was first vested in the Interstate Commerce Commission when the Mann-Elkins Act of June 18, 1910 (36 Stat. 544), extended the definition of "common carrier", as used in the Interstate Commerce Act, to include telephone companies.

provisions of the Interstate Commerce Act relating to telephone companies, but provided that all outstanding orders of the Interstate Commerce Commission issued under these repealed provisions should continue in effect until modified or superseded by the Communications Commission (Secs. 602 (b), 604 (a)).

The Interstate Commerce Commission first exercised authority over telephone company accounts in December 1912, when it prescribed a uniform system of accounts effective January 1, 1913. (R. 19.) These accounting rules remained in effect, substantially without change, during the next 20 years. (*Ib.*) They were superseded by a revised system of accounts (sometimes referred to herein as the 1933 System of Accounts) promulgated by the Interstate Commerce Commission in November 1932 and effective, except as to very small companies, January 1, 1933. The order of the Commission prescribing these accounts and the accounts themselves are set forth in full in the record. (R. 345–456.) Certain objections to the accounts were filed by a number of State regulatory commissions. (R. 15–16.) The Interstate Commerce Commission, after the enactment of the Communications Act but before its effective date (Sec. 607), issued a report on these objections but no order. (R. 15–84.)

The Communications Commission authorized the filing of objections to the foregoing report of the

Interstate Commerce Commission; held a hearing on these objections; adopted a "draft of a Uniform System of Accounts" which it submitted to all interested parties; entertained exceptions to these accounting rules, which exceptions were considered at a conference with representatives of the telephone companies and of the state commissions; and on June 19, 1935, issued the order prescribing the system of accounts under attack in this case. (R. 91–92.) These accounts (hereinafter sometimes referred to as the 1936 System of Accounts) and the order putting them in effect are set forth in full in the record. (R. 85–220.)

The parties stipulated to submit the case for final decree upon the pleadings and the affidavits filed in support of and in opposition to plaintiffs' application for an interlocutory injunction. (R. 552–553, 559.) Five affidavits were so filed by the Bell companies (R. 307, 317, 324, 331, 334), one by the Associated companies (R. 457), six by the Communications Commission (R. 468, 484, 500, 523, 531, 544), and affiants for the Bell companies submitted rebuttal affidavits reaffirming certain of their original conclusions and statements (R. 553–557). All of the affidavits deal with the interpretation and effect of the 1936 System of Accounts.

The District Court unanimously held that the accounting rules prescribed by the Communications Commission are not, with two minor exceptions, arbitrary, unreasonable, or such as to deprive appellants of rights guaranteed by the Fifth

Amendment. (R. 561–572.) The court filed, pursuant to Equity Rule 70½, findings of fact (R. 573–578, 583–584) and conclusions of law (R. 578–583). The accounting provisions which appellants challenge have been stayed pending the appeal to this Court.

ARGUMENT

I

THE LIMITED GROUNDS UPON WHICH APPELLANTS MAY ATTACK THE ORDER OF THE COMMISSION

This Court has said that in a suit to set aside an order of the Interstate Commerce Commission the only questions which are open for review are whether there have been "violations of the Constitution, or of the power conferred by statute, or an exercise of power so arbitrary as virtually to transcend the authority conferred." *Kansas City Southern Ry. Co.* v. *United States,* 231 U. S. 423, 440. In such a proceeding the court may not "under the guise of exerting judicial power, usurp merely administrative functions by setting aside a lawful administrative order upon our conception as to whether the administrative power has been wisely exercised." *Interstate Commerce Commission* v. *Illinois Central R. R. Co.,* 215 U. S. 452, 470.

When the Commission is exercising delegated legislative power to prescribe the accounts to be kept by common carriers (*Interstate Commerce Commission* v. *Goodrich Transit Co.;* 224 U. S. 194), there is a wide range for the exercise of ad-

ministrative judgment and discretion with which the courts will not interfere by substituting their judgment for that of the administrative body. An attack upon an order prescribing accounts "is, and must be, rested at bottom upon the contention that the regulations embodied in it are so entirely at odds with fundamental principles of correct accounting as intrinsically to manifest an abuse of power.". *Kansas City Southern Ry. Co.* v. *United States, supra,* p. 444. The question presented is whether the regulations of the Commission "do violence to" generally accepted principles of accounting, that is, whether they are "so clearly contrary to these and other applicable principles that they should be set aside as being in excess of the powers conferred by Congress upon the Commission." *Ib.,* p. 447. It is not enough that the court is of the opinion that the accounting rule "ought to be" other than that prescribed; this is not "a sufficient ground to declare that the Commission had abused its power." *Ib.,* p. 456.

These principles have been recently reaffirmed and restated. In *Norfolk & Western Ry. Co.* v. *United States,* 287 U. S. 134, 141, involving the validity of an accounting order of the Interstate Commerce Commission, the Court said:

> Within broad limits that body's determination is necessarily beyond revision and correction by the courts. * * * Whether the Commission should make special classifications to fit exceptional cases lies within the

> discretion conferred, and courts ought not to be called upon to interfere with or correct alleged errors with respect to accounting practice. If we were in disagreement with the Commission as to the wisdom and propriety of the order, we are without power to usurp its discretion and substitute our own.

Since, as this Court said in the *Norfolk & Western* case (p. 143), the test of validity is whether the order is so "arbitrary and outrageous" as to "amount to an abuse of power", those vested with administrative authority to prescribe accounting rules may determine controverted questions in more than one way. In the present case the Interstate Commerce Commission expressed an adverse opinion upon certain accounting rules which the Communications Commission subsequently adopted, but it does not follow that the decision of the latter body is therefore "arbitrary and outrageous". That it is not, but is, on the contrary, well within the zone of reasonableness and therefore within the scope of administrative discretion would seem a fair inference from the fact that the order of the Communications Commission is actively supported (R. 562; Fg. II, R. 574) by an association representing some 46 state public utility regulatory bodies.[2]

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[2] The order of the Michigan Public Utilities Commission of December 3, 1935, referred to in the brief of additional appellants (p. 8), did not "reject" the 1936 System of Accounts. The order was entered after the filing of the present suit, which sought a stay order and temporary injunction

Appellants contend that the order of the Commission is so arbitrary that it amounts to a denial of due process. This suit was brought before the order had gone into effect. In large part the arbitrary characteristics of the order asserted by appellants rest upon disputed interpretations of the meaning of the order. If the Commission, in administering the order, adopts the meaning and interpretation which its witnesses place upon the order, most of the constitutional questions raised by appellants will never require adjudication. Unless or until the Commission adopts or threatens to adopt a construction of its order which might render it invalid, no constitutional right of appellants is infringed. "In the circumstances, no case is presented, either by pleadings or proof, calling on a fedeal court of equity to rule upon the correctness of some other construction which may never be adopted." *Edelman* v. *Boeing Air Transport, Inc.*, 289 U. S. 249, 253. This Court has rigidly adhered to the rule "never to anticipate a question of constitutional law in advance of the necessity of deciding it." *Steamship Co.* v. *Immigration Commissioners,* 113 U. S. 33, 39. See *Abrams* v. *Van Schaick,* 293 U. S. 188; *Wilshire Oil Co., Inc.* v. *United States,* 295 U. S. 100.

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against the 1936 System of Accounts. The order of the Michigan Commission merely revoked a prior order under which this System would automatically have become the accounting rules of the Michigan Commission.

II

THE ORIGINAL COST PROVISIONS ARE WITHIN THE COMMISSION'S STATUTORY AUTHORITY AND THEY DO NOT INFRINGE RIGHTS GUARANTEED BY THE DUE PROCESS CLAUSE OF THE FIFTH AMENDMENT

1. THE ORIGINAL COST PROVISIONS

The meaning, effect and purpose of the original cost provisions of the Commission's order will appear more clearly if the comparable provisions of the 1933 System of Accounts are first set forth. In this system a single balance-sheet account, 100, covers telephone plant. Account 100 is the total of the primary telephone plant accounts, 201 to 280, inclusive, and it includes both property in telephone service and that held under a definite plan for such service. (R. 378.) The primary telephone plant accounts include such intangibles as those represented by account 201, "Organization", and account 202, "Franchises"; they also include account 280, "Construction work in progress", and account 278, "Undistributed cost of property". (R. 393.) When property "in use in telephone service" is purchased from another public utility, the accounting is as follows: (1) the appropriate primary plant accounts are charged on the basis of land at "estimated current value", tangible personalty at "current cost new", franchises at "original cost", and construction work in progress

at "cost";[3] (2) depreciation and amortization reserves are credited with the estimated reserve requirements applicable to the plant; and the difference between the net of (1) and (2), on the one hand, and, on the other hand, the cost of the property to the accounting company is credited or debited to account 278. (R. 365–366.) To state the matter more simply, what goes into account 278 is the difference between the present value of the property acquired (franchises being valued at original cost) and the amount paid to acquire the property.

Since account 100 is the sum of the primary telephone plant accounts, one of which is account 278, under this system the full amount paid another utility for telephone property is included in the balance-sheet account covering telephone plant, irrespective of whether it is proper under sound accounting principles to capitalize the entire expenditure. Moreover, amounts entered in account 278 may continue there indefinitely whether such asset value as this investment may have originally represented continues to exist or not. This is so because amounts in account 278 are not subject to depreciation charges and because the accounting company is not required to amortize balances in

[3] In lieu of these charges, the accounting company may, with the approval of the Commission, charge to its primary plant accounts the amounts carried on the books of the vendor with respect to the property purchased. (R. 366.)

278 although it is given the option of doing so (account 413, R. 414) by debiting surplus.

Under this system the balance-sheet account representing telephone plant may be inflated by transfers between controlled companies, in which transactions price is a matter of indifference since they involve a mere shift of assets from the parent company's left hand pocket to its right hand pocket. (R. 536.) Furthermore, such transfers may be made the medium for writing up the primary telephone plant accounts, on which depreciation charges are based, to current cost new. The extent of such write-ups rests largely in the discretion of the accounting company. It is well known that appraisals of reproduction cost vary widely and appraisals made simply for the purpose of entering transactions on the books of account are not subjected to the check of adversary proceedings.[4] The fact that write-ups of this character are permitted destroys the trustworthiness of the accounts from the standpoint of investors and makes them unreliable for use in arriving at original cost of construction, a recognized relevant factor, to be considered along with other relevant factors, in determining value in rate litigation. *Smyth* v. *Ames,* 169 U. S. 466, 547; *McCardle* v.

[4] "Many so-called 'appraisals' are little more than estimates and the values obtained by them have no substantial basis." Montgomery, *Auditing Theory and Practice*, 5th Ed., p. 278.

Indianapolis Water Co., 272 U. S. 400, 410–411; *Los Angeles Gas & Electric Corp.* v. *Railroad Commission*, 289 U. S. 287, 306.[5]

The nature of the telephone business is such that it is, and for efficient operation must be, a territorial monopoly; in fact it is substantially a nation-wide monopoly. Accordingly, such telephone property as is acquired from another utility is usually acquired from a controlled or affiliated company.[6] The opportunities for possible abuse permitted by the 1933 System of Accounts in connection with such acquisitions is therefore a matter of primary importance.

Another defect in the 1933 System of Accounts is that there is no uniformity in the basis on which property is carried in the primary telephone plant

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[5] The phrase which this Court has used is "original cost of construction". In the case of property dedicated to the public service, cost at the time of first dedication (the Commission's definition of original cost) is the practical equivalent of original cost of construction. In the *Los Angeles* case cited above, where there had been no change in ownership, original cost of construction and cost to the owner were the same, and both forms of expression were used. Obviously, the amount which a *subsequent* owner pays to acquire property is not the same as original cost of construction.

[6] Of the total property acquired from other utilities by the Bell Companies since 1915, two-thirds has been acquired from companies, all or substantially all the stock of which was owned by Bell Companies. (R. 336.) The remaining one-third was acquired "partly from affiliated and partly from independent companies". (*Ib.*)

accounts and therefore no uniformity in the basis on which depreciation charges are computed. Property constructed by the accounting company or purchased from non-utilities is carried at cost. Property purchased from another utility since January 1, 1933, is carried either at reproduction cost new or at the amount shown on the books of the predecessor company. "Going or completed plant" purchased before January 1, 1933, is carried on varying bases, as indicated below.[7]

The 1936 System of Accounts splits up the balance-sheet account representing telephone plant into four balance-sheet accounts. Account 100.1 is limited to property "used in telephone service". Account 100.2, "Telephone plant under construction", represents a transfer of account 280 (1933 System) from the primary telephone plant accounts to a balance-sheet account. Account 100.3, "Property held for future telephone use", is a segregation into a separate balance-sheet account of telephone property not in use but held for such

[7] Instruction 13 (p. 33) of the Uniform System of Accounts for Telephone Companies, First Issue, effective January 1, 1913, provided that when a going or completed plant was purchased, the constituent elements should be charged to the appropriate plant accounts at structural value (estimated cost of reproduction less depreciation) if the consideration given exceeded total structural value; and that if the consideration did not exceed such value, it should be distributed through the accounts in proportion to the structural value of the constituent elements appropriate to the respective accounts.

use. (R. 123.) Property is to be carried in these three accounts, as well as in the primary telephone plant accounts, at "original cost", which is defined as the cost of the property "at the time when it was first dedicated to the public use, whether by the accounting company or by a predecessor public utility". (R. 101, 122–123, 144–156.) Such original cost and cost to the accounting company is the same except when property is acquired from another utility. In the case of such acquisitions the difference between cost to the accounting company and original cost (less depreciation applicable at date of acquisition) is credited or debited to balance-sheet account 100.4, "Telephone plant acquisition adjustment". (R. 123.)

As the District Court said (R. 567), account 100.4 "performs a function similar to" account 278. There is entered in each account the difference between the amount paid to acquire property from another utility and the amount which under the accounting rules is chargeable to primary telephone plant accounts. But the 1936 System of Accounts, in line with the other changes adopted for the purpose of rendering the balance-sheet statement more informative, makes the account a separate balance-sheet item instead of leaving it buried among the primary telephone plant accounts.

Paragraph (B) of 100.4 provides that the account shall be subdivided according to the character of the amounts contained therein and paragraph (C) provides (R. 124):

> The amounts recorded in this account with respect to each property acquisition shall be disposed of, written off, or provision shall be made for the amortization thereof in such manner as this Commission shall direct.

2. THE SEGREGATION OF AMOUNTS REPRESENTED BY ACCOUNT 100.4 INTO A SEPERATE BALANCE-SHEET ACCOUNT IS NOT ARBITRARY

Appellants assert (Br., p. 22) that the Commission's order requires accounts to be kept on a basis which will not show the accounting company's own actual costs, but the costs of some prior owner. We submit that the order does not have this effect. What it does is to require that, in the case of property already in public service acquired from another utility, the original cost of such property shall be shown in one set of balance-sheet accounts (100.1, 100.2, 100.3) and the difference between such original cost and cost to the accounting company in another balance-sheet account (100.4).

A public utility does not have a constitutional right to any particular classification of its property investment. *Norfolk & Western Ry. Co.* v. *United States*, 287 U. S. 134, 143. Appellants therefore have the burden of establishing that it is plainly unreasonable to segregate in a separate balance-sheet account the portion of their property investment represented by account 100.4. Appellants not only fail to sustain this burden, but the segre-

gation in question can be shown to be reasonable upon a number of grounds.

Purchases of going telephone property from another utility are, with rare exceptions, not purchases of individual articles, such as a coil of wire, a certain number of telephone poles, or a particular underground cable, but they are purchases of another company's entire assets or of its entire assets in a given territory. The amount paid in such acquisitions is always subject to the possibility of distortion if, as is usually the case, the property is acquired from a controlled or affiliated company, and in the case of acquisitions from independent companies there are so many extraneous factors affecting price (*infra,* pp. 34–38) that the amount paid is an unreliable index of the investment in telephone plant as such. To segregate in certain accounts the original cost furnishes investors with precise and accurate data as to the basis upon which the amount of the investment represented by these accounts is computed. To set forth separately on the balance sheet an account which represents the difference between the cost to the owner and original cost, where there is such a difference, likewise furnishes investors and other interested parties with more complete information than if this difference were concealed in a single balance-sheet account covering telephone plant. From the standpoint of correct accounting, account 100.4 appropriately belongs among the balance-sheet accounts. (R. 473.)

The segregation in question, in addition to being enlightening to investors, will also provide accurate, current data as to one of the factors ordinarily considered in a rate case. (*Supra*, pp. 17–18.) Certainly any accounting rule which tends to diminish the delays attendant upon rate litigation is eminently reasonable.[8] The classification therefore aids the Commission in performing more expeditiously one of the most important duties imposed upon it by the Act, the determination and prescription under Section 205 (a), *infra*, p. 71, of just and reasonable charges for the services rendered by carriers subject to the Act. The segregation is also in aid of the authority given to the Commission by Section 213, *infra*, p. 72, to value the property of carriers subject to the Act, paragraph (c) of this section authorizing it to require the carrier to file a statement showing "the original cost at the time of dedication to the public use" of the carrier's property.

Even if the reasonableness of the segregation were far less clear than it is, it would not transcend either the Commission's statutory authority or constitutional limits. In *Kansas City Southern Ry. Co.* v. *United States*, 231 U. S. 423, 456, this Court,

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[8] The rate litigation before this Court in *Lindheimer* v. *Illinois Bell Telephone Co.*, 292 U. S. 151, extended over a period of more than ten years and involved the collection from customers of many millions of dollars of excess charges which ultimately had to be refunded to them. See also *St. Joseph Stock Yards Co.* v. *United States*, 298 U. S. 38, 84, 88–92.

in sustaining an accounting order of the Interstate Commerce Commission, said:

> But, did we agree with appellant that the abandonments ought to be charged to surplus or to profit and loss, rather than to operating expenses, we still should not deem this a sufficient ground to declare that the Commission had abused its power.

Appellants, apparently recognizing the weakness of an attack upon the original cost provisions based simply upon the classification of investments which they enforce, make the further contention that, once the Commission has exercised the power reserved in paragraph (C) of account 100.4 to write off or to amortize amounts therein, the balance-sheet accounts will not show the company's total investment in telephone plant. In so far as the Commission directs amortization, its action is merely an application of the familiar accounting principle that there should be accruing charges to income or surplus to create a reserve sufficient to offset the property loss which ensues when property, whether tangible or intangible, outlives its usefulness and is no longer an asset of continuing value. With reference to possible write-offs directed by the Commission, it must be assumed in this preliminary attack upon the order before it has gone into operation, that write-offs will be directed only in those instances where the expenditure in question should not, under sound accounting principles, be capitalized as an asset. That

there are expenditures of this character is shown later. (*Infra,* pp. 32–38.) The writing off of such amounts has the effect of showing the company's actual investment in telephone plant, by eliminating what might otherwise be improperly included therein. Thus the Commission's order, so far from producing, as appellants contend, a distorted or untrue picture of the company's plant investment, in fact operates to prevent a distorted or misleading picture.

The Director of Research and Valuation for the New York State Public Service Commission expressed the opinion that if the information proposed to be shown by accounts 100.1, 100.2, 100.3 and 100.4 had been available to investors in public utility securities, the inflation in the prices of these securities during the 1920–1929 period, "based in many cases upon the publication of balance sheets showing investments in operating property far in excess of the original cost of such investments, would have been materially less than actually occurred, with resulting material decrease in the losses sustained by investors in the period since 1929." (R. 535.)

Under any accounting system the balances in the plant accounts at any given time are likely to correspond only approximately to the amount expended for plant. For example, under the 1933 System of Accounts, after exercise of the option to amortize, by debits to surplus, account 278, "Undistributed cost of property", and account 201,

"Organization", the balances in the plant accounts will not show the amount actually expended for plant.

3. ACCOUNT 100.4 IS NOT A SUSPENSE ACCOUNT

In the 1936 System of Accounts the balance-sheet accounts on the asset side are grouped under four headings: "Investments," "Current Assets," "Other Assets," "Prepaid Accounts and Deferred Charges." (R. 121.) The grouping in the 1933 System of Accounts was similar. (R. 376–377.)

The first group, as its designation "Investments" implies, consists of relatively permanent assets and the accounting rules are carefully framed to maintain this characteristic of the accounts included therein. For example, property in the telephone plant accounts is that "which ordinarily has a service life of more than 1 year" (Instruction 20 (A), R. 107) and account 101.2, "Advances to affiliated companies," which is in the "Investments" group, comprises advances which are to be funded or which are not subject to current cash settlement (Instruction 3 (M), R. 101). Not only does the classification of account 100.4 in the investment group indicate that it represents assets of a semi-permanent character, but it is given a sub-number under the main account number covering telephone plant. If the Commission had regarded this account as a suspense account or had intended others to so regard it, it would have been included in the

group of balance-sheet accounts designated "Prepaid Accounts and Deferred Charges."

Appellants, in contending that account 100.4 is a suspense account, treat the account as if items therein would permanently remain in the same contingent status as when they are first entered. It may be true that at that moment such items are subject to the contingency that the Commission will require them to be written off by a charge to surplus. But the statement in the accounting rules "shall be disposed of," etc., in accordance with the directions of the Commission presupposes that the Commission will make prompt disposition of these amounts. Once the Commission has acted as thus provided, amounts which it requires to be written off will be extinguished from the account and the balance remaining in the account will thereafter represent investment in assets of just as real and permanent a character as those represented by the other telephone plant balance-sheet accounts, 100.1, 100.2, and 100.3.

The basis for the preceding statement is as follows: Apart from writing off, the Commission may provide for amortization or it may provide for other disposition of amounts in 100.4. If it provides for amortization, it will direct that over a given period of time a charge be made to operating expense or to surplus and a corresponding credit to amortization reserve and that, at the end of such period, the sum of these charges be debited to amortization reserve and credited to account 100.4.

During this period the amount for which amortization is provided has as much the character of an investment asset as has property which is subject to depreciation charges.[9] The other kind of investment represented by 100.4, as, for example, excess value of land over and above original cost, will consist of amounts as to which the Commission has directed that they be retained in the account.

The supposititious balance-sheet set forth in the brief of additional appellants (p. 16) is based on testimony of one of appellants' witnesses that a balance sheet would be incomplete if it failed "to call specific attention on its face to the fact that the Commission must extinguish this item [account 100.4] and may extinguish it immediately." (R. 320.) As we have already shown, the statement that the Commission *may* extinguish the account is correct in the sense that at the moment amounts are first entered therein, some or all of them may be extinguished, but is substantially incorrect as applied to the status of the account after the Commission has given the directions which the accounting rules call for.[10] The statement that the Com-

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[9] Such property remains in the plant account at the original amount charged thereto until its retirement, when plant account is credited and depreciation reserve is debited.

[10] In the case of any balance sheet published before the Commission had so acted, if it would be sound accounting practice to append a note to account 100.4, the note could be so amplified as to guard against giving investors or others a misleading impression as to the character of the account.

mission *must* extinguish account 100.4 is based upon a misinterpretation of its order.

The Commission's chief accountant stated that the proper interpretation of account 100.4 was that amounts therein "would be disposed of, after the character of the item had been determined, in a manner consistent with the general rules underlying the uniform system of accounts for the distribution of expenditures, according to their character, to operating expenses, income, surplus, *or remain an investment.*" (R. 476.) Another accounting officer of the Commission declared that appellants' assumption that amounts in 100.4 must be extinguished is "unwarranted" and "fails to express the provisions of the Revised System of Accounts." (R. 518.) The acting director of the accounting department of the Wisconsin Public Service Commission, which had prescribed for electric utilities an account comparable to 100.4, expressed the opinion that, in view of the provision for subdividing this account according to the character of the amounts therein, amounts in 100.4 "might be *permanently retained in the investment accounts,* depreciated or amortized over the life of the property, or subject to such other disposition as might be appropriate." (R. 527.) He also said that after the Commission knows the facts it may then issue appropriate directions "for the *retention* or the disposal of the account in accordance with the principles set forth in the system of accounts." (R. 528.)

Appellants' argument that a reserve of surplus must be maintained against account 100.4 presupposes that the Commission will arbitrarily and improperly direct that *all* amounts in this account be written off, irrespective of their nature. This argument, as the District Court said, "requires the assumption that the Commission will act improperly in the future under 100.4 (*c*). This cannot be presumed." (R. 568.) If the Commission should in the future improperly order a write-off, the carrier could protect its rights by contesting the validity of this order in the courts.

Appellants stress the word "adjustment" in the title of account 100.4. But the inclusion of this account among those grouped as "Investments" and its exclusion from those grouped under the heading "Prepaid Accounts and Deferred Charges" removes any possible ambiguity arising from use of this word.

Appellants place great reliance upon *Matter of New York Edison Co.* v. *Maltbie*, 244 App. Div. 685, affirmed *per curiam* 271 N. Y. 103. The uniform system of accounts for electric corporations prescribed by the New York State Public Service Commission contained a definition of original cost similar to that in the 1936 System of Accounts and provided for entering amounts in account 143 on the same basis that amounts are entered in account 100.4. But account 143 differed radically from account 100.4. The former was a true sus-

pense account. Its title was "Suspense to be amortized." It appeared among the balance-sheet accounts under the heading "Deferred Debits", a group corresponding to those set forth under the heading "Prepaid Accounts and Deferred Charges" in the 1936 System of Accounts. There was entered in account 143 not only amounts equivalent to those entered in account 100.4, but also miscellaneous debit items subject to amortization by order of the Commission and losses from property retirements not provided for in the depreciation reserves.

Account 143 differed from account 100.4 in another important respect. Amounts in account 143 were to be "written off" over such period and in such manner as the Commission might prescribe; in other words, the account was to be written off in its entirety out of surplus. By way of contrast, the 1936 System of Accounts authorizes disposition of amounts in account 100.4 according to the character of the individual items—by an immediate write-off out of surplus, by amortization through debits to surplus over a period of years (*infra*, pp. 45–46), by amortization through charges to operating expense over a period of years (*id.*), by indefinite retention in this telephone plant investment account. This flexibility, the court below said, "distinguishes the system at bar from that held invalid in" the *New York Edison* case. (R. 568.)

While the Government does not assent to all of the reasoning of the New York Appellate Division, the holding itself, so far as it involves the original cost provisions of the order of the New York Commission, is clearly distinguishable.

4. THE PROVISION THAT THE COMMISSION MAY DIRECT THAT PART OF THE EXPENDITURE MADE TO ACQUIRE THE PROPERTY OF ANOTHER UTILITY BE WRITTEN OFF IS REASONABLE AND WITHIN THE COMMISSION'S STATUTORY AUTHORITY

Additional appellants appear to contend that account 100.4 (C) is void in so far as it authorizes the Commission to direct the writing off of amounts in this account. They assert in their brief (p. 14) that the Commission "has no power to require these appellants to write off and take as a loss a part of what they actually paid for their property." Since the Commission has not as yet directed the writing off of any amount, the contention necessarily is that the Commission is wholly without statutory authority to prescribe an accounting rule the effect of which is to deny the right to capitalize, under any and all circumstances, the entire amount expended in the acquisition of property of another utility. The contention is without merit unless such a rule is so utterly inconsistent with accepted accounting principles that it cannot be said to be an accounting rule which the statute authorizes the Commission to prescribe.

The Commission, when it prescribes a system of accounts, is not exercising its rate-making power

but, as shown later (*infra*, pp. 57–58), its power to prescribe accounts includes the power to establish accounts which will aid it in carrying out its other statutory duties, including that of prescribing reasonable rates and charges. We therefore submit that the Commission is authorized to prescribe accounts which accord with the principles enforced and applied in rate proceedings. Particularly is such action authorized if it serves to make effective another principle which this Court has recognized as within the power to prescribe accounts, namely, to make the accounts correspond with the substance of the transactions they record (*Kansas City Southern Ry. Co.* v. *United States*, 231 U. S. 423, 440, *infra*, p. 63).

There is no hard and fast, immutable line between expenditures which properly may be capitalized and those which may not. The extent to which it is proper to capitalize overhead expenses during construction is a frequent source of controversy and wide differences of view in rate proceedings. See *Los Angeles Gas & Elec. Corp.* v. *Railroad Commission*, 289 U. S. 287, 294, 310. The question of whether an expenditure may be capitalized or not is no different in principle from the question of when and under what circumstances an expenditure once capitalized should be extinguished from capital account. The latter was the principal issue presented in *Kansas City Southern Ry. Co.* v. *United States*, 231 U. S. 423. The price paid for

the purchase of property in transactions between controlled companies is no criterion as to what should be entered into the capital account of the purchasing company. (R. 536.) Where buyer and seller are under common control, part of the purchase price for equipment may be excluded from the purchaser's property account in a rate proceeding. *Lindheimer* v. *Illinois Bell Telephone Co.*, 292 U. S. 151, 157.

It must also be borne in mind that even when the transaction is between independent companies the amount paid to acquire going telephone property may frequently be in excess of every element of value inherent in the property, including going-concern and good-will value. Since the modern telephone system, if it is to function efficiently, must be closely coordinated and unified with respect to both physical facilities and operating policies, an independent concern may have a very substantial "nuisance" value enabling it to command a price in excess of actual value.

Tri-State Telephone & Telegraph Co. Proposed Control, 180 I. C. C. 229, illustrates this nuisance value. The Tri-State owned the telephone exchanges in St. Paul and a Bell company those in Minneapolis. From a plant and engineering standpoint the two telephone properties constituted one telephone exchange area and the same operating practices had to be observed in both cities if delays, inefficiency and undue cost were to

be avoided. The two companies had been only partially successful in satisfactorily coordinating service, and the difficulties in doing this were increasing and promised to become much more serious. The Bell company believed that independent operation of the St. Paul exchange constituted a serious hazard to its Minneapolis investment. Accordingly, it agreed to buy substantially all the Tri-State stock for $19,510,101. This price was more than double the appraised value of the assets represented by the stock, excluding organization expenses and going value, and more than 150% of such value if these intangibles were included. The difference between price and value was so great that the Commission refused to issue a certificate that the acquisition would be in the public interest.[11]

If the foregoing transaction had been carried out and the Bell Company had then taken over the Tri-State property, the cost thereof would have been the amount paid for the stock, or over 50% more than every element of value attaching to the assets acquired, including intangibles. Under the 1933 System of Accounts this excess would go into

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[11] Within fifteen months of this decision an agreement was reached for the sale to the Bell Company of the Tri-State stock for approximately $7,000,000 less than the price previously agreed upon and the Commission thereupon issued a certificate of public interest under Section 5 (9) of the Interstate Commerce Act. *Tri-State Telephone & Telegraph Co. Control*, 193 I. C. C. 383.

account 278, and therefore into the balance-sheet account representing telephone plant, unless the company *voluntarily* amortized all or a part of the excess by debiting surplus. An accounting system which permits this kind of an inflation of the telephone plant account impairs its integrity. We do not contend that payments in excess of value for going telephone concerns or their property may not be justified from a business standpoint, but that the excess payment should be charged against past or future profit and loss, either by an immediate debit to surplus or by amortization chargeable to surplus over a period of time. Furthermore, such charges should not be left to the discretion of the accounting company, but should be subject to the control of the regulatory body whose duty it is to prescribe uniform accounts and to see that they are carried out in accordance with their intended purpose and effect.

Acquisition of Control of Northwestern Long Distance Telephone Co., 71 I. C. C. 530, is another instance where the purchase price was largely dictated by nuisance value. A Bell company agreed to pay $545,000 for the property of a company operating toll lines between exchanges all of which were reached by the Bell company's toll lines. The latter's facilities were ample to handle the business of both companies for years to come. The value to the purchaser of the property to be acquired was

therefore only its junk or salvage value, as the Commission recognized by stating that the investment could be amortized in a few years' time out of the additional revenues to be obtained from business formerly handled by the competitor.

An accounting system which provides that a company may, whatever the circumstances, record its telephone plant on its balance sheet in terms of the money, plus the value of any consideration other than money,[12] exchanged for telephone plant, conceals data which is truly informing and supplies that which is likely to be misleading. *Acquisition of Illinois Southern Telephone Co.*, 145 I. C. C. 43, illustrates this situation. A new company was to be formed to buy all the assets of four existing telephone companies (the stockholders of which were identical), giving in exchange therefor cash (derived from sale to the public of certain amounts of its bonds and preferred stock) and 40,000 shares of its common stock. In substance, therefore, there was a mere recapitalization involving no change in beneficial ownership, but "cost" to the new company was the cash which it had paid out and the value attributable to its common stock. The almost untrammeled latitude afforded the company's officers and accountants in determining *ex parte* such

[12] See Instruction 20 (B) of the 1933 System of Accounts (R. 365) and account 100.4, par (A), of the 1936 System of Accounts (R. 123).

common stock value is obvious [13] and the opportunity afforded to mislead investors is equally obvious. Although the Interstate Commerce Commission refused to issue a certificate of public interest, upon the ground that the proposed financing "would increase largely the securities outstanding in the hands of the public without the addition of any property", the transaction was carried out under approval given by the Illinois Commerce Commission (H. Rept. No. 1273, 73d Cong., 2d Sess., p. XIX).[14]

Possibly appellants will urge that public regulation of acquisitions of telephone property is adequate to guard against abuse and that therefore no good reason exists for the adoption of an accounting rule which permits the Commission to direct the writing off of part of the consideration given for telephone property acquired from another utility. There are a number of grounds why such a contention must be rejected.

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[13] The Illinois Commerce Commission, in approving the acquisition, apparently made no independent examination of the property appraisals which were submitted to it and apparently assumed that the no-par common stock would be capitalized at the minimum of $5 a share required by Illinois law. (145 I. C. C. 43, 45.) Actually, the new company capitalized its common stock at eight times this amount, $40 a share. (Poor's Public Utilities Manual, 1929, p. 1300.)

[14] The company making the acquisition is not an appellant, but it is controlled by the same holding company as the additional appellants. (Moody's Public Utilities Manual, 1935, p. 510.)

The question of possible state regulation may be summarily put aside. The Federal Government is not constrained to withhold exercise of its constitutional powers because the individual states may step into the breach if it does not act. The very purpose of Federal control within the interstate commerce field is to achieve uniformity in regulation, which cannot be achieved under the varying regulatory provisions (or none at all) of the laws of the several states.

Such regulatory powers as are or have been vested in the federal Government are inadequate to meet the purposes of the accounting provision in question. Section 221 (a) of the Communications Act, *infra,* p. 72, and the preceding Section 5 (18) of the Interstate Commerce Act, which relate to consolidations of property of two companies and acquisitions of stock or leasehold control, do not *require* federal approval of these transactions; they merely provide that any federal law making the transaction unlawful shall not apply to a transaction approved thereunder. Section 214 (a) of the Communications Act, *infra,* p. 72, makes it unlawful to acquire or operate a telephone "line" without a certificate from the Commission, but there was no similar provision applicable to telephone companies in the Interstate Commerce Act. (Compare Sec. (1) 18 of that Act.) Accordingly, in the case of property acquisitions prior to the summer of 1934, there was no necessity for obtain-

ing federal approval unless the acquisition might otherwise fall within the prohibitions of the federal antitrust laws. But apart from this consideration, there is no reason why such regulatory control as these statutory provisions authorize should not be supplemented by an appropriate exercise of the Commission's power to regulate accounts. The disparity between price and the value of the property acquired need not be so great so as to make the transaction not in the public interest, even though the price might be in excess of every element of value which it would be proper to carry in capital account as a continuing asset.

5. PARAGRAPH (C) OF ACCOUNT 100.4 IS NOT INVALID BY REASON OF THE FACT THAT IT DOES NOT ITSELF LAY DOWN THE RULES BY WHICH THE COMMISSION WILL ACT IN DIRECTING THE WRITING OFF, OTHER DISPOSITION, OR AMORTIZATION OF AMOUNTS IN THIS ACCOUNT.

Paragraph (C) of account 100.4 provides that amounts in this account shall be written off, disposed of, or amortized according to the directions of the Commission. Apart from the contention already considered that this operates to make account 100.4 a suspense account, appellants attack this provision (Br., pp. 27–31), not on unconstitutional grounds, but on the ground that it is beyond the Commission's statutory authority. The contentions seem to be (1) that when an accounting regulation fails to state specifically the rule or rules in accordance with which amounts entered

therein shall be ultimately disposed of, it does not constitute an accounting rule of the kind contemplated by the statute and (2) that the authority given the Commission to prescribe a system of accounts does not include the authority to reserve to itself power of control over the disposition of particular items. The two contentions are so interrelated that no attempt will be made to consider them separately.

There is no doubt that account 100.4 clearly specifies the accounting requirements which it imposes. Paragraph (A) sets forth the exact method whereby amounts to be entered in the account shall be determined. Paragraph (B) requires a subdivision of these amounts according to their character. Paragraph (C) provides that the company shall follow the directions given by the Commission as to the subsequent disposition of amounts recorded in the account. A rule which leaves the accounting company in no doubt as to what entries it should make in its books of accounts would seem to constitute a valid exercise of the authority given by the Act to prescribe the forms of accounts and records to be kept by carriers subject to the Act.

Appellants do not assert that the Commission is without authority to exercise regulatory power with respect to accounting for particular items or transactions. Any such contention would be plainly erroneous; no system of accounts can be framed in such detail that it can be applied with-

out further intervention or interpretation by the regulatory body.[15] Such a contention would also be directly inconsistent with the power exercised by the Interstate Commerce Commission over a long period of time, under identical statutory authority, to direct the accounting entries to be made in recording a particular transaction or particular property, an exercise of power which has received the approval of this Court. *Norfolk & Western Ry. Co.* v. *United States,* 287 U. S. 134. See also *Atlanta, Birmingham & Coast R. R. Co.* v. *United States,* 296 U. S. 33; *Chesapeake & Ohio Ry. Co.* v. *United States,* 5 F. Supp. 7; *Accounting of New York Telephone Co.,* 188 I. C. C. 83; *Acquisition of Property by Saratoga & Encampment Valley R. R. Co.,* 192 I. C. C. 719.

Since, therefore, the statute gives the Commission some authority to direct the disposition of particular items, the question here presented concerns the possible limits of this authority. Are those limits transcended if the Commission, as to the class of transactions which come within account 100.4, fails to announce in advance the rules in accordance with which it will direct disposition of

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[15] In Accounting Bulletin No. 11, issued June 26, 1916, effective July 1, 1916, the Interstate Commerce Commission embodied the more important rulings and interpretations which it had made in administering the uniform system of accounts for telephone companies, effective January 1, 1913. The Bulletin consists of 176 "Cases" set forth in the form of "Query" and "Answer".

amounts in this account? We submit that the answer to this question depends upon whether or not, under all the circumstances affecting proper accounting for the class of transactions in question, the failure to lay down advance rules is manifestly without reasonable justification. If this is so, the situation under consideration is altogether different from that which appellants suggest (Br., p. 29) as analogous, namely, "an order merely providing that all entries shall be made as the Commission, in its discretion, may direct".

In view of the multitude of factors affecting proper accounting for amounts in account 100.4, a rule which attempted to specify in advance in what manner each such amount should ultimately be recorded would seem so likely to prove inequitable and unduly rigid in practice that the rule would be far more open to the charge that it was arbitrary than one which reserves to the regulatory body necessary flexibility in dealing by appropriate proceedings with the facts and circumstances presented in individual cases as they arise.

In the accounts for electric utilities prescribed by the Wisconsin Public Service Commission there is an account termed "Fixed Capital Purchase Adjustment" comparable to account 100.4. The acting director of the Department of Accounts and Finance of that Commission stated that he had found that the nature of the items entering into this comparable account differed according to the

facts in individual cases, and that under such conditions it was "practically impossible to make a uniform rule with respect to the disposition of amounts" in such an account. (R. 528.) He added that, when the facts were known, appropriate directions might then be issued "for the retention or the disposal of the account in accordance with the principles set forth in the system of accounts". Another Commission witness stated that the reservation of power to deal with individual property acquisitions was "necessary in order that limitations may not prevent proper regulation". (R. 490.)

Moreover, it cannot be assumed that the Commission, in acting under paragraph (C), is without standard or guide. The entire body of accounting rules furnishes the controlling principles in accordance with which it will exercise its authority. The situation is not dissimilar to that considered in *New York Central Securities Co.* v. *United States,* 287 U. S. 12, 24, where the carrier urged that authority given the Interstate Commerce Commission to approve acquisitions of control which it found to be in the "public interest" was an unconstitutional delegation of legislative power because the statute furnished no standard to guide determination of this question. This Court said that a sufficient standard was to be derived from the "purpose of the Act, the requirements it imposes, and the context of the provision in question". In like man-

ner, the purpose of the system of accounts adopted by the Communications Commission, the requirements which the system imposes, and the context of paragraph (C), together with the general principles of correct accounting, supply a standard by which the Commission may determine the directions it should give as to the writing off, amortization, or other disposition of amounts in 100.4.

6. SINCE THE COMMISSION'S ORDER PERMITS AMORTIZATION CHARGEABLE AS AN OPERATING EXPENSE OF AMOUNTS IN ACCOUNT 100.4, IT PROTECTS ANY SUBSTANTIVE RIGHT WHICH APPELLANTS MAY HAVE TO CHARGE DEPRECIATION AGAINST AMOUNTS IN THIS ACCOUNT.

Appellants contend that the Commission's order is arbitrary because it does not permit depreciation charges against amounts included in account 100.4. The account is to be subdivided according to the character of the items which it contains and the Commission may direct that provision be made for amortization of amounts in this account. The Commission may therefore provide for amortization of such amounts in the account as may be properly classified as investment in depreciable property. This depreciable property investment would appropriately be subdivided upon the basis of the classifications in the primary plant accounts and amortization might be provided on a basis equivalent to the depreciation rate applicable to the particular property classification.

The Commission's order provides for amortization chargeable as an operating expense (account 613, R. 186) and amortization by debits to surplus (account 413, R. 167). Both classes of amortization charges are credited to amortization reserve (account 172, R. 140), which specifically provides that it shall also be credited with any amounts resulting from amortization of balances in account 100.4. Both of the accounting officers of the Commission whose affidavits were received in evidence stated that paragraph (C) permitted amortization chargeable as an operating expense. (R. 476, 512, 517, 520.) Another Commission witness expressed the same view (R. 537) and the District Court (R. 568) likewise adopted this interpretation. We therefore submit that the evidence establishes that the Commission's order permits amortization of amounts in 100.4 through a charge to operating expense. If, however, there were uncertainty as to the correctness of this construction and if a contrary construction might appear to infringe appellants' constitutional rights, the uncertainty is removed by application of the familiar rule that in interpreting statutory provisions or administrative regulations, if two constructions are possible, one of which would give rise to serious constitutional doubts and one of which avoids such doubts, the latter construction will be adopted. *Addy Co.* v. *United States,* 264 U. S. 239, 245.

The fact that the Commission might possibly apply its order in an unconstitutional manner does

not, in advance of such improper application, deprive appellants of property without due process. Nor are they deprived of any substantive right if, by means of amortization, provision may be made for the building up of a reserve, through charges to operating expense, which will protect their property investment.

The District Court rejected the contention that the failure to allow depreciation as such against amounts in 100.4 made the original cost provisions arbitrary, saying (R. 568–569):

> This complaint anticipates arbitrary action by the Commission, under 100.4 (c) which authorizes handling of this item through amortization. The effect would be the same as writing down through depreciation, and until the Commission acts so that the accounts become so contrary to the principles of correct accounting as to constitute the Commission's order arbitrary and unreasonable, the Commission is within its powers.

What is essential from the standpoint of the principles of sound accounting in the matter of depreciation is that some provision be made for an annual charge to income which will build up a reserve against which may ultimately be charged the loss ensuing when the serviceable life of depreciable property has expired and the property is scrapped. Whatever basis is used for determining this annual charge, whether replacement cost at time of acquisition or original cost or current value from year to year (cf. *United Railways* v.

West, 280 U. S. 234), there is not, and in the nature of the case there never can be, any assurance that the reserve accumulated will exactly correspond to the cost of replacing the property at the particular time when it reaches the end of its useful life.[16] As Commissioner Eastman observed in *Telephone and Railroad Depreciation Charges,* 177 I. C. C. 351, 381, "Accounting is not an exact science." We submit that there is no violation of the constitutional guarantee of due process if, in the case of property placed in public service by another utility and subsequently acquired from it, depreciation charges as such are calculated on the basis of the original cost of the property to the company first placing it in public service.

In practically every such acquisition, what is acquired is not specific pieces of depreciable property but rather a going plant or business for which a lump sum is paid. This lump sum is obviously measured by the value of the going plant or business as a whole. It therefore practically never corresponds to the value of the specific items of depreciable property acquired, on whatever basis they are valued. The value or cost to the purchaser of the depreciable property acquired is merged or lost in the total price paid for the acquired business as a whole. The problem is there-

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[16] See *Knoxville* v. *Knoxville Water Co.*, 212 U. S. 1, 13–14, where it was said that the purpose of depreciation charges was to make provision from earnings for replacing the property at the end of its life.

fore presented as to what method shall be employed for setting up the cost of the individual units of depreciable property on the books of the purchaser as a basis for annual depreciation charges.

One possible method is that provided by the 1933 System of Accounts, namely, to enter the depreciable property on the books of the purchaser at the estimated replacement cost of each item at the date of the acquisition and to base depreciation on these figures. This is essentially artificial because it rests on the fiction that what was purchased at the time of the acquisition was the specific items of property at the price for each item then prevailing in the market, whereas in reality what was purchased was a going business as a whole without specific regard for the particular units of property. This method of accounting is also open to the practical objection that it affords opportunity for improper inflation of depreciation charges, since there can be no adequate administrative check upon appraisals of replacement cost at excessively high figures. Another possible method, that adopted in the 1936 System of Accounts, is to record the individual units of property at their cost when first devoted to the public service, i. e., at the same figures which served as the basis for depreciating those items when they were in the hands of the former owner. This means that each such item of property will continue to be depreciated after the acquisition on the same basis as before without permitting the sale of the business

as a whole to alter the basis of depreciation of the specific items of depreciable property.

We submit that there is no violation of any constitutional right in requiring the use of the latter method of calculating depreciation for accounting purposes instead of the former. Appellants seem to contend that depreciation must be based on cost to the owner in whose hands the property is being depreciated and that, where property already in public service is acquired by a subsequent owner, the cost to the latter is replacement cost at the moment of the acquisition. Irrespective of the validity of this contention as applied to the purchase of specific items of property as such, it clearly has no application where the property transferred is part of a going business for which a lump sum is paid, since it is purely artificial to say that the specific items of property are included in the lump sum price at the figures which represent the respective replacement costs of these individual items in the open market.

Irrespective of whether depreciable property is set up on the books and depreciated on the basis of its original cost or on the basis of its artificial replacement cost at the actual moment of transfer as part of a going business, the real and substantial question is this: What disposition shall be made of the difference between such original cost or replacement cost, on the one hand, and the lump-sum acquisition cost of the business as a whole, on the

other hand? This problem exists whichever basis is adopted for recording the depreciable items. Under the 1933 System of Accounts, this difference goes into account 278, where it remains as a permanent asset item unless the accounting company voluntarily amortizes it by debiting surplus. Under the 1936 System of Accounts, the difference goes into account 100.4 and, as already shown, such part of the difference as should properly be amortized by charging operating expenses may be so amortized. For example, if in a particular case a part of the excess of the lump sum paid for the business as a whole seems fairly attributable to the fact that there has been a rise in the open-market price of some or all of depreciable items of property of the kind included in the purchase, then it would obviously be appropriate to amortize such part of the excess out of current operating expenses. On the other hand, such part of the excess as appears to be attributable to the business advantage of acquiring a going concern at somewhat more than its individual assets are actually worth may appropriately be amortized by debiting surplus. It may well be that this method of dealing with the sums in question may be considered as not ideally the best method, but we submit that it is a method within the bounds of reasonableness and therefore not so inherently arbitrary as to violate the constitutional guarantee of the Fifth Amendment.

Additional appellants contend (Br., pp. 20–22) that the failure to make specific provision for de-

preciation on amounts in account 100.4 is in conflict with the requirements of Section 220 (b) of the Act, *supra,* pp. 4–5. That section provides that the Commission shall, as soon as practicable, prescribe the "classes of property" for which depreciation charges may be included under operating expenses. The section, except for immaterial changes in verbiage, is the same as language added to Section 20 (5) of the Interstate Commerce Act by Section 435 of the Transportation Act, 1920 (41 Stat. 493). As pointed out in *Telephone and Railroad Depreciation Charges,* 177 I. C. C. 351, 360–369, this amendment was not in derogation of, but in confirmation of, the general powers over accounts previously vested in the Interstate Commerce Commission (in language identical with Section 220 (a) of the Communications Act), and the major purpose of the amendment was to bring about a fuller exercise of existing power with reference to depreciation charges.

There are two possible interpretations of Section 220 (b), neither of which aids appellants. If prescribing the "classes of property" on which depreciation may be charged embraces the power (1) to determine the classes of property which are depreciable and (2) to determine the base on which depreciation shall be computed as to property classified as depreciable, the Commission's order constitutes an exercise of both these powers and is therefore not in conflict with Section 220 (b).

There is no implication in the language of the section that the Commission, if it lays down rules as to the depreciation base, must establish the same base for all property of the same class, irrespective of the manner of its acquisition. If, however, the authorization in Section 220 (b) is interpreted as confined to classifying property according to whether it is or is not depreciable, then determination of the depreciation base—a necessary incident to the power to prescribe rules covering depreciation charges—flows from the Commission's general power over accounts and is not affected by or in conflict with Section 220 (b).

7. THE ORIGINAL COST PROVISIONS ARE NOT INVALID BY REASON OF THE COST OF COMPLIANCE.

A regulation validly imposed in the exercise of public regulatory authority is not rendered invalid because compliance therewith will subject the utility to additional expense. Cost of compliance is not even relevant to the question of validity unless, possibly, when such cost is shown to be entirely disproportionate to any public benefit which may reasonably follow from the regulation. Whether the public benefit justifies the cost of compliance presents a problem calling for the exercise of administrative judgment and where such a question is presented the courts decline to substitute their judgment for that of the body charged with execution of the law.

We submit also that appellants have not shown that the original cost provisions are unduly burdensome. They refer to the estimate that the cost to the Bell companies of putting these provisions into effect would be "several millions of dollars." (R. 341.) The only estimate which was based upon a detailed study of the work involved is to the effect that the cost to the New York Telephone Company would be $432,100. (R. 332.) Since the *net* operating income of this company was over $32,000,000 in 1935 (Moody's Public Utilities Manual 1936, p. 182), this cost would be only a little over 1% of such income. Moreover, this is not an annual, recurring cost. Once the property now held is restated on the basis of original cost, accounting for future acquisitions from utilities would probably be less costly than at present because, except as to the few companies not subject to the Commission's order, the vendor's books will show original cost and the purchaser will take over the property at these book amounts.

There is no reason to suppose that the Commission will be unduly exacting in the identification of property subject to restatement on the basis of original cost. Its order provides that in accounting for retirement of telephone plant, "average" original cost shall be used in determining the original cost of the items retired when "it is impracticable to determine the original cost of each item due to the relatively large number

or small cost of such items." (Instruction 25 (D), R. 114.) The Commission may be expected to permit the use, in appropriate cases, of the same principle of averaging for determining to what extent property previously acquired from other utilities is still in existence.

Congress has authorized the Commission to require telephone companies to file with it a statment showing original cost of their property. (Sec. 213 (c).) The grant of this authority amounts to a legislative determination that to require the furnishing of this information is not unreasonably burdensome.

III

THE PROVISION THAT THE CHARGES TO CERTAIN ACCOUNTS SHALL BE JUST AND REASONABLE AND THAT PAYMENTS IN EXCESS THEREOF SHALL BE CHARGED AS A NON-OPERATING EXPENSE IS NOT ARBITRARY OR UNREASONABLE

Instruction 2 (B. 1) provides (R. 98):

> All charges to the accounts prescribed in this classification for telephone plant, income, operating revenues, and operating expenses shall be just and reasonable and any payments by the company in excess of such just and reasonable charges shall be included in account 323, "Miscellaneous income charges".

We subscribe to appellants' statement (Br., p. 37) that net operating income is "one of the most

vital items in the companies' statements, of wide interest to investors and others". 'But their further statement: "Whether an outlay of an operating expense was reasonable or unreasonable, being paid and non-recoverable, it nevertheless is an outlay which should enter into the computation of net operating income," rests upon the untenable proposition that any amount, however unreasonable, which a controlling company exacts in payment for services or property should be charged in full to operating expense. In such circumstances the excess payment is not a true expense of operation or a true item of cost of property, but is special tribute levied by reason of corporate control. If this tribute is accounted for as operating expense or is added to telephone plant account (thereby increasing depreciation charges, an operating expense), the statement of net operating income on the books of account is falsified by the inclusion therein of items which ought to be a charge against non-operating income. (R. 513.)

All but a small fraction of the country's telephone business is performed by holding company systems so that amounts paid for telephone plant and for services chargeable to operating expense are "in a large part paid to affiliated companies and are not results of arms-length transactions". (R. 539.) In rate litigation, charges for services and for property, in transactions between companies in the same system, are recognized, in the com-

putation of operating income and of property devoted to the public service, only to the extent that the charges are reasonable. *Smith* v. *Illinois Bell Telephone Co.*, 282 U. S. 133; *Lindheimer* v. *Illinois Bell Telephone Co.*, 292 U. S. 151; *Dayton Power & Light Co.* v. *Public Utilities Commission*, 292 U. S. 290; *Columbus Gas & Fuel Co.* v. *Public Utilities Commission*, 292 U. S. 398. In the litigation before the Court in the two telephone cases it was found that the average annual overpayments to the parent company for services during a five-year period had amounted to $545,443 and that equipment had been purchased from a subsidiary of the same parent at prices in excess of what was reasonable. (292 U. S. 151, 157, 165.)

One of the duties of the Communications Commission is to prescribe just and reasonable charges for telephone companies. (Sec. 205.) It is also specifically authorized to examine into transactions which relate to the furnishing of equipment supplies, research, services, finances, etc., which may affect carriers' charges for the services which they render. (Sec. 215 (a).) In *Norfolk & Western Ry. Co.* v. *United States*, 287 U. S. 134, the carrier, in challenging an order which required it to classify certain coal mines as non-transportation property, contended (pp. 138–139) that the general discretion given the Interstate Commerce Commission to prescribe a uniform system of accounts was limited by the purposes and ends for which such

accounts are to be kept, as exhibited in other sections of the Act. This Court adopted this as a proper test to apply and one of the grounds (pp. 140–141) upon which it affirmed the Commission's order was that two other sections of the Act "draw the very distinction" between transportation and non-transportation property which the accounting rule in question had long enforced.

In *Kansas City Southern Ry. Co.* v. *United States,* 231 U. S. 423, the Court gave as a reason for sustaining an accounting order, that it would aid the Commission in the performance of other of its statutory duties. The Court said (p. 445):

> Since the regulation of the railroad carrier by the public authority, and especially the fixing of the rates to be charged, depend primarily upon two fundamental considerations, (a) the value of the property that is employed in the public service, and (b) the current cost of carrying on that service, it is clear that the maintenance of a proper line of distinction between property accounts and operating accounts is essential to the execution by the Interstate Commerce Commission of the supervisory and regulatory powers conferred upon it by Congress.

See also *Interstate Commerce Commission* v. *Goodrich Transit Co.,* 224 U. S. 194, 211, 213–214, 216.

Since the power to prescribe uniform accounts "includes the power to inquire into expenditures and their proper assignment in the accounts" and

"power to prevent evasion * * * and detect in any formal compliance or in the assignment of expenses a 'possible concealment of forbidden practices'" (*Smith* v. *Interstate Commerce Commission*, 245 U. S. 33, 43, 45), the power clearly exists to prescribe accounting rules designed to prevent evasion before the event rather than after. This is the purpose and effect of the provision as to just and reasonable charges. It enables the Commission to perform in a practicable manner the duty resting on it to see that accounts subject to its jurisdiction truly reflect the transactions which they purport to record. Without this power, the burden of determining whether entries recording transactions between affiliated companies represent a true statement of operating income, operating expense or telephone plant account "would be such as to destroy all effective regulation"; each and every such entry would have to be audited by the Commission "before any credence whatsoever could be attached to it." (R. 539.)

The regulation in question is therefore justified on two grounds, first, as an aid in the performance of other duties which the statute imposes upon the Commission and, second, as a reasonable means for making effective a cardinal principle of any accounting system promulgated by a regulatory body, that the accounts shall faithfully represent the substance of the transactions which they record (*infra*, p. 63).

Appellants assert (Br. p. 37) that the statute makes failure to comply with an accounting order of the Commission a penal offense and assert (Br., p. 38) that the obvious purpose of the accounting rule as to just and reasonable charges "is to allow the Commission, through fear of criminal prosecution, to impose its judgment on the company as to the reasonableness of every outlay".

Appellants do not specify the penal provisions to which they refer. Section 220 (e), *supra*, pp. 5–6, and Sections 501 and 502, *infra*, pp. 73–74, which sections contain the only penal provisions which might be applicable, are limited to acts done "wilfully and knowingly" or "wilfully". It is clear that, in the absence of actual bad faith, an entry of a charge in excess of an amount which was subsequently determined to be just and reasonable would not be the wilful or knowing violation condemned by these sections. In addition, Section 220 (d), *supra*, p. 5, provides a forfeiture, which under Section 504, *infra*, p. 74, is recoverable in a civil suit, if a carrier fails or refuses to keep such accounts as the Commission shall prescribe and in the manner prescribed by it. In any proceeding under this section the defendant would be free to make the defense, if it is a valid one, that "just and reasonable" is not a sufficiently definite standard to support a money forfeiture.

The provisions of Section 220 (d) are almost identical with those of Section 20 (6) of the Interstate Commerce Act. Although the latter section

has been in effect since 1906 (Act of June 29, 1906, 34 Stat. 594), the only reported case under this section, *United States* v. *Clyde S. S. Co.*, 36 F. (2d) 691, certiorari denied 281 U. S. 744, was a proceeding, not for failure to keep accounts as prescribed, but for refusal to permit the Commission to inspect accounts and records.

The Interstate Commerce Commission endeavors to adjust infractions of its accounting rules through correspondence or conference and, if necessary, issues a report, but usually not an order, indicating the correction to be made. *United States* v. *Atlanta, Birmingham & Coast R. R. Co.*, 282 U. S. 522. If the carrier still resists, the Commission issues an order, the legality of which may be tested in a suit to set it aside. *Norfolk & Western Ry. Co.* v. *United States, supra; Atlanta, Birmingham & Coast R. R. Co.* v. *United States*, 296 U. S. 33. We submit that it is improper to assume that the Communications Commission will proceed in any less reasonable or orderly manner, or that the forfeitures authorized by Section 220 (d) will operate to coerce appellants into submission to the will of the Commission.

The requirement that the charges to certain accounts shall be just and reasonable materially affects only a very limited class of transactions. Typical of these are contracts under which a holding company furnishes services to subsidiaries or under which one company supplies equipment to

another, both being under common control. Since the terms of such contracts are usually uniform for all affiliated companies, the reasonableness of the charges thereunder can be readily removed from the area of doubt by presenting the matter to the Commission pursuant to Instruction 9 (R. 104). After it issues its directions or order, the contents of the words "just and reasonable" and the obligation of the company with respect thereto are precise and definite. As was said of a tax which was attacked as failing to define the scope of the obligation, but which might be clarified by administrative action, "The demands of due process are satisfied if reasonably clear definition is afforded in time to give the taxpayer an opportunity to comply." *Pacific Tel. & Tel. Co.* v. *Seattle,* 291 U. S. 300, 304.

We also submit that the words "just and reasonable" furnish an adequate guide to the obligations which the requirement in question imposes. The District Court pertinently observed (R. 571) that the cases such as *United States* v. *Cohen Grocery Co.,* 255 U. S. 81, upon which appellants rely, are distinguishable because the statutory provisions there held to be too vague or indefinite were "without the specialized content of the word 'reasonable' with regard to charges involved in the determination of rates." (R. 571.) The words "just and reasonable" or their opposite "unjust and unreasonable" are repeatedly used in defining obligations imposed by the Interstate Commerce

Act. See Sections 1 (5), 1 (6), 1 (11), 1 (12), 15 (1), 15 (2), 15 (6), 15 (7).

The requirement that the charges to certain accounts shall be just and reasonable does not give the Commission the power to "require recording what the Commission may think should have been done, instead of what actually occurred." (App. Br., p. 38.) The real question at issue is whether form rather than substance shall determine what "actually occurred" and whether the company shall be the final arbiter of this question.

Insistence that accounts shall correspond to the substance of the transactions which they record does not amount to giving the Commission power to interfere in management. In *Kansas City Southern Railway Co.* v. *United States,* 231 U. S. 423, 440, the carrier argued that the authority to prescribe uniform accounts was confined to regulation of their form and that regulation which dealt with substance, that is, with the accounting required in particular circumstances, would constitute unauthorized interference with management. This Court said (pp. 440–441):

> The very object of a system of accounts is to display the pertinent financial operations of the company, and throw light upon its present condition. If they are to truly do this, the form must correspond with the substance. * * * There is no direct interference with the internal affairs of the corporation; and if such interference indirectly

> results, it is only such as is incidental to the lawful control of the carrier by the Federal authority * * *.

See also *Norfolk & Western Ry. Co.* v. *United States,* 287 U. S. 134, 143; *Interstate Commerce Commission* v. *Goodrich Transit Co.,* 224 U. S. 194, 211.

IV

THE PROVISIONS GOVERNING CLASSIFICATION OF PHYSICAL PROPERTY ARE NOT ARBITRARY OR UNREASONABLE

One of appellants' grounds of attack is that the distinction between accounts 100.1 and 100.3 is so indefinite as to be arbitrary. Account 100.1 embraces the property "used in telephone service" and account 100.3 is designated as "Property held for future telephone use." (R. 123.) The alleged ambiguity concerns the word "used" in account 100.1 in its relation to "spare" plant, that is, subsidiary parts of a larger unit, such as a cable, switchboard, underground duct, etc. which may be temporarily not in use (R. 342, 556). We submit that whatever ambiguity, if any, once existed, has been dispelled by the evidence presented in this case. Each of the Commission's witnesses (except one, who failed to state his interpretation), including the Commission's chief accountant and its chief accountant in a telephone investigation undertaken pursuant to a Senate Resolution, definitely interpreted account 100.1 as including such spare plant.

(R. 482, 509, 529, 538, 549.) The District Court likewise made a finding to this effect. (Fg. XVI, R. 577.)

The point stressed by the Commission's witnesses was that property is used in service, although subsidiary parts thereof are not being used to full capacity and that the Commission's order does not require any segregation between an operating unit of property and its component parts. Appellants (Br., p. 46) refer to the testimony of the Commission's chief accountant that account 100.1 would include "necessary spare plant" (R. 482), but this witness placed no special emphasis upon the word "necessary." Moreover, he stated that periodical transfers between account 100.1 and account 100.3 "will not be required by reason of seasonable changes or fluctuating demands for plaintiffs' services." (R. 482.)

Appellants suffer no substantial injury by reason of the alleged ambiguity. The Commission's order, as modified by the decree, allows depreciation charges against property in account 100.3. (R. 585.)

Appellants' other attack upon the classification of physical property is that the distinction between accounts 100.3 and 103 is so vague as to be arbitrary. Both the 1933 and 1936 Systems of Accounts distinguish between operating and non-operating property. In the former system, account 100 includes property used in telephone service or "held under a definite plan" for such service

and account 103 includes all physical property not covered by account 100. (R. 378–379.) In the latter system, there are four balance-sheet telephone plant accounts, but only account 100.3, which applies to property "held for imminent use in telephone service under a definite plan for such use", is here material. (R. 123.) Account 103 includes all physical property not included in the balance-sheet telephone plant accounts. Under both systems, therefore, property which is not in use or under construction is not included in telephone plant unless it is held under a "definite plan" for use in telephone service. The 1936 System of Accounts adds the additional qualification that the property be held for "imminent" use in such service.

The 1933 system seems defective in classifying property as operating property merely because it is held under a definite plan for telephone service. It is highly commendable to plan for future needs, but all property acquired under such a plan, even though the plan is definite, is not operating property, whether the test be what would popularly be regarded as such or what would be included in the rate base in a rate proceeding. Whether the Commission, in undertaking to narrow the earlier definition, made the wisest possible choice of terms in adding the requirement as to "imminent" use is immaterial. Appellants have no constitutional right to a particular degree of definiteness of meaning in the terms employed to define the contents

of an account. The words "definite plan" are not without elements of ambiguity. The word "imminent" will acquire precision through interpretation by the Commission. Unless it is improperly assumed that the Commission will be wayward or inconsistent in its interpretations (see App. Br., p. 43), just as great a degree of uniformity will ensue under these interpretations as if the concept had been elaborated and expanded in the account itself.

This Court has used the word "imminent" in defining the line between property which may be included in the rate base and that which may not. *Columbus Gas & Fuel Co.* v. *Public Utilities Commission,* 292 U. S. 398. A company which was selling natural gas to an affiliated company obtained its supply from tracts of land held under lease. It also held leases on other tracts, some proven and some not proven, which were not in production but which represented a source of future supply when its producing tracts should be exhausted some three years or more later. This Court, in discussing which of these tracts might enter into the rate base in computing a fair return for the service of furnishing gas to the affiliated company, said (pp. 406–407):

> There will be no need in the computation of the rate base to include the market or the book value of fields not presently in use, unless the time for using them is so near that they may be said, at least by analogy, to have the quality of working capital. * * *

> Leases bought with income, the proceeds of the sale of gas, and thus paid for in last analysis through the contributions of consumers, ought not in fairness to be capitalized until present or *imminent* need for use as sources of supply shall have brought them into the base upon which profits must be earned. To capitalize them sooner is to build the rate structure of the business upon assets held in idleness to abide the uses of the future. [Italics supplied.]

V

IF CERTAIN PROVISIONS OF THE COMMISSION'S ORDER SHOULD BE HELD INVALID, THE SEPARABILITY OF THE REMAINING PROVISIONS IS AN ADMINISTRATIVE QUESTION WHICH THIS COURT SHOULD NOT DECIDE

Certain of the provisions of the Commission's order which appellants attack are clearly severable from the remainder. The requirements that the charges to certain accounts shall be just and reasonable is of this nature. There is also no inseparable link between the particular classifications of physical property prescribed by the order and its other provisions. As to the part of the order relating to original cost, this is composed of a number of different provisions assailed on diverse grounds. There seems no present occasion to discuss separability from the standpoint of the possible invalidity of each provision under attack or any combination of such provisions.

To what extent the invalidity of a particular provision, or particular provisions, of the Commission's order would leave such gaps in the system of accounts as to render it unworkable is a question calling for the exercise of administrative judgment. The situation is somewhat different when a court declares the invalidity of certain provisions of a statute. If it merely strikes down the invalid provisions, those charged with enforcement of the statute will be under a duty to carry out the remainder. There is thus presented a question of statutory interpretation which it may be proper for the court to determine, namely, whether the legislative body did or did not intend that the valid provisions should remain effective notwithstanding the failure of those found to be invalid.

In the case of an administrative order such as is now before the Court, a decision limited to the holding that particular provisions are invalid leaves the regulatory body free to decide the question of separability in the light of its specialized knowledge of the administrative problems involved. The Communications Commission has no desire to put into effect an incomplete or inconsistent system of uniform accounts. What it does desire is that it should be permitted to decide in the first instance what does or does not constitute an incomplete or inconsistent system. We submit that the Court should not proceed on the assumption that the Commission will be wanting in a due regard for its responsibilities and duties or in the capacity to perform them.

CONCLUSION

It is respectfully submitted that the decree of the District Court should be affirmed.

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JOHN DICKINSON,
Assistant Attorney General.
CHARLES H. WESTON,
Special Assistant to the Attorney General.

NOVEMBER, 1936.

APPENDIX

The Act of June 19, 1934, 48 Stat. 1064 (U. S. C., Title 47, Secs. 151 *et seq.*), provides *inter alia:*

SEC. 3. For the purpose of this Act, unless the context otherwise requires—

* * * * *

(h) "Common carrier", or "carrier" means any person engaged as a common carrier for hire, in interstate or foreign communication by wire or radio or in interstate or foreign radio transmission of energy, except where reference is made to common carriers not subject to this Act; but a person engaged in radio broadcasting shall not, insofar as such a person is so engaged, be deemed a common carrier.

* * * * *

SEC. 205. (a) Whenever, after full opportunity for hearing, upon a complaint or under an order for investigation and hearing made by the Commission on its own initiative, the Commission shall be of opinion that any charge, classification, regulation, or practice of any carrier or carriers is or will be in violation of any of the provisions of this Act, the Commission is authorized and empowered to determine and prescribe what will be the just and reasonable charge or the maximum or minimum, or maximum and minimum, charge or charges to be thereafter observed, and what classification, regulation, or practice is or will be just, fair, and reasonable, to be thereafter followed, and to

make an order that the carrier or carriers shall cease and desist from such violation to the extent that the Commission finds that the same does or will exist, * * *.

* * * * *

SEC. 213. (a) The Commission may from time to time, as may be necessary for the proper administration of this Act, and after opportunity for hearing, make a valuation of all or of any part of the property owned or used by any carrier subject to this Act, as of such date as the Commission may fix.

* * * * *

(c) The Commission may at any time require any such carrier to file with the Commission a statement showing the original cost at the time of dedication to the public use of all or of any part of the property owned or used by said carrier. * * *

* * * * *

SEC. 214. (a) No carrier shall undertake the construction of a new line or of an extension of any line, or shall acquire or operate any line, or extension thereof, or shall engage in transmission over or by means of such additional or extended line, unless and until there shall first have been obtained from the Commission a certificate that the present or future public convenience and necessity require or will require the construction, or operation, or construction and operation, of such additional or extended line * * *.

* * * * *

SEC. 221. (a) Upon application of one or more telephone companies for authority to consolidate their properties or a part thereof into a single company, or for authority for

one or more such companies to acquire the whole or any part of the property of another telephone company or other telephone companies or the control thereof by the purchase of securities or by lease or in any other like manner, when such consolidated company would be subject to this Act, the Commission shall fix a time and place for a public hearing upon such application * * *. After such public hearing, if the Commission finds that the proposed consolidation, acquisition, or control will be of advantage to the persons to whom service is to be rendered and in the public interest, it shall certify to that effect; and thereupon any Act or Acts of Congress making the proposed transaction unlawful shall not apply. * * *

* * * * *

SEC. 402. (a) The provisions of the Act of October 22, 1913 (38 Stat. 219), relating to the enforcing or setting aside of the orders of the Interstate Commerce Commission, are hereby made applicable to suits to enforce, enjoin, set aside, annul, or suspend any order of the Commission under this Act * * *, and such suits are hereby authorized to be brought as provided in that Act.

* * * * *

SEC. 501. Any person who willfully and knowingly does or causes or suffers to be done any act, matter, or thing, in this Act prohibited or declared to be unlawful, or who willfully and knowingly omits or fails to do any act, matter, or thing in this Act required to be done, or willfully and knowingly causes or suffers such omission or failure, shall, upon conviction thereof, be punished for such offense, for which no

penalty (other than a forfeiture) is provided herein, by a fine of not more than $10,000 or by imprisonment for a term of not more than two years, or both.

SEC. 502. Any person who willfully and knowingly violates any rule, regulation, restriction, or condition made or imposed by the Commission under authority of this Act, * * * shall, in addition to any other penalties provided by law, be punished, upon conviction thereof, by a fine of not more than $500 for each and every day during which such offense occurs.

* * * * *

SEC. 504. The forfeitures provided for in this Act shall be payable into the Treasury of the United States, and shall be recoverable in a civil suit in the name of the United States, * * *.

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No. 74

In the Supreme Court of the United States

OCTOBER TERM 1936

AMERICAN TELEPHONE AND TELEGRAPH COMPANY ET AL., APPELLANTS

v.

THE UNITED STATES OF AMERICA, FEDERAL COMMUNICATIONS COMMISSION, AND NATIONAL ASSOCIATION OF RAILROAD AND UTILITIES COMMISSIONERS

BRIEF FOR FEDERAL COMMUNICATIONS COMMISSION

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BRIEF FOR FEDERAL COMMUNICATIONS COMMISSION

STATEMENT

An adequate statement of the case appears in other briefs, and for this reason we have not included a general statement herein.

The outline of this brief follows generally the topical arrangement suggested by appellants in their Statement of Points (R. 600); and against propositions advanced in said statement, Federal Communications Commission presents the following:

ARGUMENT

I

THE ORIGINAL COST PROVISIONS OF THE UNIFORM SYSTEM OF ACCOUNTS FOR TELEPHONE COMPANIES, PRESCRIBED BY THE FEDERAL COMMUNICATIONS COMMISSION, ARE *Not* VOID

The Uniform System of Accounts assailed in this suit was established by the Federal Communications Commission under authority of Section 220 of the Communications Act of 1934, which is comparable with Section 20 of the Interstate Commerce Act.

The appellants, in the trial court, challenged the validity of the system of accounts on three general grounds; (1) Violation of their constitutional rights, (2) want of conformity to statutory authority, and (3) such unreasonable and arbitrary exercise of power as to transcend authority conferred.

Decisions of the Supreme Court clearly show the powers exercised by the court in deciding issues founded upon the three grounds above stated.

In *Interstate Commerce Commission* v. *Illinois Central Railroad Co.*, 215 U. S. 452, 470, which involved the amenability of the Illinois Central Railroad Company to an order of the Interstate Commerce Commission regulating the distribution of coal cars during periods of car shortages,

the court, after recognizing the grounds for judicial interference, said:

> Plain as it is that the powers just stated are of the essence of judicial authority, and which, therefore, may not be curtailed, and whose discharge may not be by us in a proper case avoided, it is equally plain that such perennial powers lend no support whatever to the proposition that we may, under the guise of exerting judicial power, usurp merely administrative functions by setting aside a lawful administrative order upon our conception as to whether the administrative power has been wisely exercised.

In *Norfolk and Western Railway Co.* v. *United States et al.*, 287 U. S. 134, on an appeal from a decree of a district court dismissing a petition to enjoin the enforcement of provisions of an order of the Interstate Commerce Commission which required the appellant to keep its accounts in accordance with the prescribed system of accounts applicable to issues therein raised, this court, among other things, said:

> The Commission's order is challenged as in excess of the statutory grant of power. The concession is made that Section 20 of the Act grants a discretion to prescribe a uniform system of accounts, the manner in which they shall be kept, and the forms thereof. The appellant, however, asserts that this discretion is limited by the pur-

> poses and ends for which such accounts are to be kept, as exhibited in other sections of the Act. * * * (*id.*, p. 138–9).
>
> * * * * *
>
> With great earnestness the appellant characterizes the order as in several aspects a denial of due process. It declares that by virtue of the Commission's mandate an unfair and improper rate base is fixed, and a capital asset properly to be taken into account for purposes of recapture is eliminated. But this is to ignore the fact that the order is one touching accounting merely; that before any rate base can be ascertained or any basis of recapture determined the carrier will be entitled to a full hearing as to what property shall be included; and not until the Commission excludes the assets in question from the calculation may the carrier assert the infliction of injury to its rights of property. * * * (*id.*, p. 141).
>
> * * * * *

In the same case in the lower court, reported in 52 F. (2d) 967, 970, the court said:

> * * * The Commission is vested by Congress with full power and authority to require reports from carriers and to prescribe the form of the accounts which they shall keep. * * * *What these forms shall be, and what items shall be allocated under particular subdivisions thereof, are obviously matters which must rest in the discretion of the commission; and the courts will not interfere with the exercise of that*

> *discretion, unless such exercise is so manifestly arbitrary and unreasonable as to transcend the commission's powers:* [Italics supplied.]

The Federal Communications Commission had authority to prescribe the Uniform System of Accounts, and the order promulgating the System is immune from annulment unless it be found to be so manifestly arbitrary and unreasonable as to transcend the powers of the Commission—and, not then, unless it injuriously affects property rights.

This statement is well supported in cases heretofore cited, furthermore:

In *Kansas City Southern Railway Co.* v. *United States et al.*, 231 U. S. 423, counsel for said railway company made all the objections against the order involved there that are made in the case at bar. Mr. Justice Pitney, speaking for the court, began the statement of the case as follows (p. 437):

> The contention of appellant in the Commerce Court and in this court is that the regulations of the Interstate Commerce Commission relative to the method of keeping the accounts of common carriers, so far as they are here questioned, are unreasonable, beyond the power or authority of either Congress or the Commission, and violative of the Fifth Article of Amendments to the Constitution of the United States, as being a deprivation of property without due process of law. * * *

The following matter appears in the course of the opinion (*id.*, p. 441):

> * * * There is no direct interference with the internal affairs of the corporation; and if any such interference indirectly results, it is only such as is incidental to the lawful control of the carrier by the Federal authority and to this the rights of stockholders and bondholders alike are necessarily subject.

The court, discussing another feature of the case, said (*id.*, p. 449–50):

> It is insisted that if the appellant, having expended in round figures $600,000, secured by the sale of bonds for improvements, can be compelled to charge $400,000 of that amount to the operating expense of one year or to distribute it among the operating expenses of a series of years, and if it be forbidden to keep any other record representing the transaction, it will have in its possession no kind of record from which it can report accurately either the cost of its property or the cost of improvements or its operating expenses. This, we think, is a misapprehension of the effect of the regulations. They do not require appellant to falsify its books or to change in any way the evidential character of the original entries. The source of the money, and the disposition made of it as expended, may and should be correctly shown. The regulations do require that the contemporaneous abandon-

> ment of other property be likewise shown, and the replacement cost, less salvage, charged to the appropriate accounts under operating expenses. This, if observed, of course results in enforcing a prescribed distinction between capital expense and operating expense. It does not require that the record of the expenditure be obliterated; but it does of course affect the results as they work out upon the balance sheet. * * *

Continuing, the court also said (*id.*, p. 456–7):

> It is further insisted that even the theory upon which the accounting regulations rest does not, when analyzed, justify a charge of abandoned property to operating expenses, but at most a charge to profit and loss. The suggestion apparently has force; but, upon consideration, we are unable to see that it furnishes ground for judicial interference with the course pursued by the Commission. * * *
>
> But, did we agree with appellant that the abandonments ought to be charged to surplus or to profit and loss, rather than to operating expenses, we still should not deem this a sufficient ground to declare that the Commission had abused its power. So long as it acts fairly and reasonably within the grant of power constitutionally conferred by Congress, its orders are not open to judicial review.

In *Chesapeake and Ohio Railway Company* v. *United States et al.*, 5 F. Supp. 7, a three-judge

case, Eastern District, Virginia, the court held (5th syllabus):

> Accounting methods prescribed by Interstate Commerce Commission for rail carriers cannot be interfered with by court except on showing that they are so entirely opposed to fundamental principles of correct accounting as to manifest abuse of power. (Interstate Commerce Act, Section 21 (1, 5), as amended, 49 U. S. C. A. Section 21 (1, 5).)

The act of prescribing a system of accounts is legislative; and the courts have only limited authority, if any, to enjoin a system of accounts.

The extent of judicial review of an act within legislative range is well described in *St. Joseph Stock Yards Company* v. *United States and the Secretary of Agriculture,* decided by the Supreme Court on April 27, 1936, 298 U. S. 38, 51, wherein the court said:

> * * * The court does not sit as a board of revision to substitute its judgment for that of the legislature or its agents as to matters within the province of either. *San Diego Land & Town Co.* v. *Jasper,* 189 U. S. 439, 446; *Minnesota Rate Cases,* 230 U. S. 352, 433; *Los Angeles Gas Co.* v. *Railroad Commission,* 289 U. S. 287, 304. When the legislature itself acts within the broad field of legislative discretion, its determinations are conclusive. When the legislature appoints an agent to act within that sphere of legislative authority, it may endow the

> agent with power to make findings of fact which are conclusive, provided the requirements of due process which are specially applicable to such an agency are met, as in according a fair hearing and acting upon evidence and not arbitrarily.

The limited authority of the courts in a suit to enjoin a commission order is very well illustrated in *Lehigh Valley R. Co.* v. *United States,* 234 Fed. 682, affirmed in 243 U. S. 412. The court, addressing itself to the question present, and speaking of the Interstate Commerce Commission in connection with its order there under consideration, said (p. 697):

> * * * its right to judge depends on the statute, and the statute in terms gives it the right to inquire and determine whether a given situation presents a case * * *. In spite of the statutory declaration of finality, the courts still retain a limited power of supervision—enough to see that constitutional requirements have been observed. * * *

The limited power there mentioned describes the authority of the court in the suit under consideration.

The same idea is fully expressed in *Chicago & Grand Trunk Railway Company* v. *Wellman,* 143 U. S. 339, 344–5, wherein Mr. Justice Brewer, speaking for the court, said:

> * * * The theory upon which, apparently, this suit was brought is that parties

> have an appeal from the legislature to the courts; and that the latter are given an immediate and general supervision of the constitutionality of the acts of the former. Such is not true. Whenever, in pursuance of an honest and actual antagonistic assertion of rights by one individual against another, there is presented a question involving the validity of any act of any legislature, State or Federal, and the decision necessarily rests on the competency of the legislature to so enact, the court must, in the exercise of its solemn duties determine whether the act be constitutional or not; *but such an exercise of power is the ultimate and supreme function of courts. It is legitimate only in the last resort, and as a necessity in the determination of real, earnest, and vital controversy between individuals.* * * * [Italics supplied.]

The pertinent provisions of the Urgent Deficiencies Appropriations Act (28 U. S. C., Sec. 43–8; 38 Stat., Chap. 32, pp. 219–20), under which the suit was tried, indicate that said Act establishes no new remedy for testing the validity of orders of commissions.

The purpose of the Act mentioned appears to be to define more clearly the manner in which the Federal Equity Courts shall exercise powers vested in them under the Constitution and laws of the United States. The aforesaid Act does not enable said courts to apply any remedy, nor to grant any

relief, different from that previously authorized in any ordinary Equity proceeding in such courts.

In *Chicago, Burlington & Quincy R. R. Co.* v. *McGuire,* 219 U. S. 549, 569, it was said:

> * * * The scope of judicial inquiry in deciding the question of *power* is not to be confused with the scope of legislative considerations in dealing with the matter of *policy.* Whether the enactment is wise or unwise, whether it is based on sound economic theory, whether it is the best means to achieve the desired result, whether, in short, the legislative discretion within its prescribed limits should be exercised in a particular manner, are matters for the judgment of the legislature, and the earnest conflict of serious opinion does not suffice to bring them within the range of judicial cognizance.

In *Borden's Farm Products Company, Inc.* v. *Baldwin,* 293 U. S. 194, 209, the court said:

> When the classification made by the legislature is called in question, if any state of facts reasonably can be conceived that would sustain it, there is a presumption of the existence of that state of facts, and one who assails the classification must carry the burden of showing by a resort to common knowledge or other matters which may be judicially noticed, or to other legitimate proof, that the action is arbitrary.

The presumption mentioned is as applicable to administrative orders as to strictly legislative

enactments. See *Pacific States Box & Basket Company* v. *White, et al.*, 296 U. S. 176, 185.

The statement of the trial court respecting the *original cost* provisions of the Uniform System of Accounts is clear and concise. We could not improve the statement. Argument to sustain it inheres in it. No amplification is needed. That court, among other things, said (R. 566):

> The requirement that original cost be set forth in accounting records of the telephone companies serves to complete the picture of value in revealing the property's financial background and showing the relationship of a carrier's monetary return to the original as well as to its own investment. It aids the Commission in its duty to determine from all the pertinent circumstances and factors, the just and reasonable rates which the carrier may exact from its service. Original cost is a relevant factor. *Smyth* v. *Ames*, 169 U. S. 466, 547; *Los Angeles Co.* v. *R. R. Comm.*, 289 U. S. 287, 306, cf. Sec. 213 (a) of the Act. The object of the system of accounts might well be to display the pertinent financial operation and throw light upon its present condition. *Kansas City Southern Ry.* v. *U. S., supra*, at p. 440. Original cost as a segregated item on a balance sheet may serve to reveal actualities which may be pertinent in fixing a rate base on the capitalized earning power of a property purchased. In making readily available facts which tend to expose discrepancies

> in valuation, it cannot be said the system is so arbitrary as to be beyond the Commission's power. Forty-seven state public utility bodies acquiesce in the proposed requirements. This is not evidence of unreasonableness.

The reasons underlying the *original cost* provisions of the Uniform System of Accounts under stay were clearly and concisely stated by Mr. W. J. Norfleet, Chief Accountant of the Federal Communications Commission, in his affidavit. See quotation on p. 32 of this brief, and for same matter see R. 470, last paragraph.

For findings and conclusions sustaining generally the defense of the Federal Communications Commission, appellee herein, see "Findings of Fact", I to XXI (R. 573–8), and "Conclusions of Law", I to XV (R. 578–83).

For testimony on behalf of the Federal Communications Commission, defendant below—appellee here, see affidavits of William J. Norfleet (R. 468–484); Robert S. Rains (R. 484–492–500); John H. Bickley (R. 500–523); Asel R. Colbert (R. 523–531); Malcolm F. Orton (R. 531–544); and Charles W. Smith (R. 544–552).

The District Court did *not* err in holding the original cost provisions valid.

103991—36——2

(a) THE ORIGINAL COST PROVISIONS DO *NOT* REQUIRE THE APPELLANTS TO KEEP THEIR PROPERTY INVESTMENT ACCOUNTS SO AS TO MISREPRESENT THEIR INVESTMENT IN PROPERTY

Appellants' telephone plants are either constructed by them, or are acquired by donation, purchase, consolidation, or merger.

If telephone plant is constructed by appellants, the following instruction in the Uniform System of Accounts, under stay pending this appeal (R. 109), enumerates the items of cost includible in their investment accounts:

> 22. *Cost of construction.*—(A) The cost of construction of property chargeable to the telephone plant accounts shall include the cost of labor, material and supplies, transportation, contract work, relief and pensions, protection, injuries and damages, privileges and permits, taxes, special machine service, interest during construction, insurance, construction services, and other analogous elements in connection with such work.

If telephone plant is donated to appellants, instruction 20 (B) of the Uniform System of Accounts (R. 107–8) provides:

> Telephone plant contributed to the company or constructed by it through expenditures of contributions of money or its equiv-

> alent shall be charged to the telephone plant accounts at its original cost (estimated if not known) and there shall be credited to the depreciation reserve and amortization reserve accounts the estimated amounts of the reserve requirements, if any, applicable to the plant. The difference between the amounts so includible in the telephone plant and the reserve accounts shall be credited to account 175, "Contributions of telephone plant."

If telephone plant is acquired by purchase, consolidation, or merger, instruction 21 (A) of the Uniform System of Accounts (R. 108) applies, to wit:

> When property in use in telephone service (note instruction 3–AA) is acquired, the amount of money actually paid (or the current money value of any consideration other than money exchanged) for the property (together with preliminary expenses incurred in connection with the acquisition) shall be charged to account 276, "Telephone plant acquired." (Note also account 139.)

Amounts are then determined with respect to the acquired property representing:

(1) Original cost of plant in service.

(2) Original cost of plant under construction.

(3) Original cost of property held for future telephone use.

(4) Depreciation and amortization applicable to the acquired property.

(5) Balance of purchase price.

The amount of item (1) is distributed among the telephone plant accounts, the total of which is included in the balance sheet in investment account 100.1, "Telephone plant in service" (R. 122–3).

The amounts of items (2) and (3) are included in the balance sheet in investment accounts 100.2, "Telephone plant under construction", and 100.3, "Property held for future telephone use", respectively (R. 123).

The amount of item (4) is included in the balance sheet in accounts 171, "Depreciation reserve", and 172, "Amortization reserve", as appropriate (R. 140).

The amount of item (5) is included in the balance sheet in investment account 100.4, "Telephone plant acquisition adjustment" (R. 123).

In paragraph (1), provision (B), under instruction 21 (R. 108), reference is made to telephone plant accounts and to items to be charged thereto. The list of telephone plant accounts is found in the Uniform System of Accounts at page 47 (R. 143), and are numbered 201 to 277.

The accounting prescribed by the aforesaid instruction 21 will result in showing in the accounts and records of carriers the following information with respect to property acquired from another utility:

1. The cost of the property to the accounting company.

2. The *original cost* (as defined in instruction 3 (S. 1) of the Uniform System of Accounts) of the telephone plant, governmental franchises, and other similar rights acquired.

3. The amounts of depreciation and amortization applicable to the property.

4. The *original cost* of telephone plant under construction at date of purchase.

5. The *original cost* of property held for future telephone use acquired in the transaction.

6. The difference between (a) the amount of item (1) and (b) the net amount of items (2) to (5), inclusive; segregated and shown separately in investment account 100.4, "Telephone plant acquisition adjustment." (See affidavit of Mr. W. J. Norfleet (R. 474–5).)

Instruction 21 of the system of accounts under stay pending this appeal (R. 108–9), and instruction 21 of the system heretofore and now in effect (R. 365–6), show that the accounts and records to be kept under this Commission's system for telephone plant purchased will disclose not only the essential information reflected in the accounts and records as kept under the present system, but will also make readily available the record of original cost of telephone plant in service at date of the balance sheet.

Furthermore, instruction 2 of the Uniform System of Accounts (R. 97), issued by the Federal

Communications Commission on June 19, 1935, provides:

> 2. *Records.*—(A) The company's records shall be kept with sufficient particularity to show fully the facts pertaining to all entries in these accounts. Where the full information is not recorded in the general books the entries therein shall be supported by other records in which the full details shall be shown and the general book entries shall contain sufficient reference to the detail records to permit ready identification. The detail records shall be filed in such manner as to be readily accessible for examination by representatives of this Commission.

The purpose of instruction 2 of the Uniform System of Accounts is to prevent concealment and misrepresentation, and under instruction 21 thereof all carriers subject to the Communications Act of 1934 are required to include in the balance sheet, as well as in the journals and other records of the companies, any cost representing the investment of the reporting company as distinguished from the *original cost* to the first owner or dedicator.

In this case, the appellants are much like the appellant in *Kansas City Southern Ry. Co.* v. *United States, et al.,* 231 U. S. 423, 449, where the court spoke of appellant's "misapprehension of the effect of the regulations," and further said of the regulations:

> * * * They do not require appellant to falsify its books or to change in any way the evidential character of the original entries. * * *

In reading a balance sheet, or the accounts of a company, to determine the facts concerning a particular item, several accounts must often be combined. A separation of the accounts, for the purpose of more accurately indicating the character of the items included therein, is not only reasonable, but is essential, and does not in any way impair the integrity of the balance sheet showing. The mere matter of increasing or decreasing the number of balance sheet accounts may not turn on legal grounds.

Amounts included in account 100.4, "Telephone plant acquisition adjustment", may represent, under differing circumstances, a portion of the amounts paid for various and sundry tangible and intangible items. However, these amounts do not, as implied by appellants and additional appellants, represent, in all instances, a portion of the carrier's investment in physical properties or in franchises, patent rights, and similar intangible rights acquired, the original costs of which are includible in the telephone plant accounts. Some amounts included in account 100.4 should not, in all instances and without variation, be subject to depreciation or amortization accounting. Such amounts may be (but admittedly not always are)

the result of watering, writing-up, or unwarranted elimination of competition. If these amounts, necessarily subject to scrutiny, can be set out separately without violation of any essential accounting principle (and they can be), the regulatory body in the exercise of due diligence should require such appropriate segregation.

In *Norfolk & Western Railway Company* v. *United States,* 287 U. S. 134, 141, the court said:

> * * * Whether the Commission should make special classifications to fit exceptional cases lies within the discretion conferred, and courts ought not to be called upon to interfere with or correct alleged errors with respect to accounting practice. * * *

The presence of an item in investment account 100.4, "Telephone plant acquisition adjustment", does not cause the accounts to misrepresent appellants' investment in property. Creation of said account 100.4 is in no way unfair or misleading, nor does it present a false picture. The absence of a separate balance sheet account in which to include these important items of public concern would necessitate the continuance of the present undesirable practice of including such items in telephone plant account 278, "Undistributed cost of property" (R. 404), which account does not appear in the balance sheet. The balance in account 278 is combined with the balances in all other telephone plant accounts under the present system,

the total of which appears in the balance sheet in one account, to wit: account 100, "Telephone plant" (R. 378).

Throughout the briefs of both appellants and additional appellants a patent effort has been made to stigmatize account 100.4, "Telephone plant acquisition adjustment", by repeated statements and implications that the account represents merely a deferred charge against surplus or a suspense account, while at page 17 additional appellants argue that the mere title of the account casts a cloud of suspicion on the items, the costs of which are includible therein.

With respect to the first contention, we submit that notwithstanding the statements of appellants, account 100.4 speaks for itself. It appears as the fourth item in the balance-sheet statement (R. 121) and is grouped with nine other accounts under the heading, "I. Investments."

The title of each account of the system (including account 100.4) is followed by the text of the account showing the nature of the items includible therein. In many instances the text of the account is followed by a list of representative items further to assist the reader. A complete system of instructions, definitions, and texts, supporting the titles of the accounts, supplemented by illustrative lists of items, preclude a just charge of misrepresentation or deceit.

With respect to account 100.4, which is derived from account 276, we bring to the attention of the court provision (B), stated below that account (R. 123–4), viz:

> This account shall be subdivided according to the character of the amounts contained therein. In addition to a copy of the journal entry recorded to open the account, the company shall file with this Commission statements showing the basis of the computation of amounts included therein. The detailed records supporting these statements shall be retained permanently by the company.

The requirements of said provision (B) very clearly and completely contradict the contention made by the appellants that any part of the cost of acquiring property which is included in account 276 (R. 157) could be concealed by segregating charges in that account into six parts and including these separate parts in the balance sheet in accounts 100.1, 100.2, 100.3, 100.4 (R. 122–3) and accounts 171 and 172 (R. 140).

In re invalidity of account 100.1 and account 100.4—the latter particularly—when account 276 is wholly ignored, it should be noticed that in *Norfolk and Western Railway Company* v. *United States et al.*, 287 U. S. 134, 142–3, it was said:

> * * * The objection now under consideration asserts merely that the company is lawfully entitled to maintain a reason-

> able system of accounting. But there is no right to a particular form of accounting as such. * * *

The appellants at pages 32 and 33 of their brief and the additional appellants at pages 18 and 19 of their brief contend that there are great differences in principle and effect between the functions of account 100.4, "Telephone plant acquisition adjustment", of this Commission's system and account 278, "Undistributed cost of property", in the system prescribed by the Interstate Commerce Commission.

A comparison of instruction 21 of this Commission's system with instruction 21 of the present system, from which instructions accounts 100.4 and 278, respectively, are derived, clearly refutes the statements of appellants on these points.

The outstanding differences between the two instructions are that under this Commission's system the *original cost* of telephone plant acquired is recorded in the telephone plant accounts, whereas under the system now in effect amounts representing *current value, current cost new, original cost,* and *residual value,* are recorded in the telephone plant accounts; and that under this Commission's system, the difference between (a) the cost to the accounting company and (b) the net of the amounts recorded in the telephone plant accounts, 100.2, "Telephone plant under construction", 100.3, "Property held for future telephone

use", and the depreciation and amortization reserve accounts, is separately shown in the balance sheet in investment account 100.4, "Telephone plant acquisition adjustment" (R. 123), whereas the residual element, under the system now in effect, is included in telephone plant account 278, "Undistributed cost of property" (R. 404), and buried in the balance sheet in the total of account 100, "Telephone plant" (R. 378). On this subject, Mr. W. J. Norfleet said (R. 473):

> In my opinion Account 278, "Undistributed cost of property", is improperly classified in the present system of accounts as a telephone plant account. It is more appropriately includible as a separate balance sheet account. In many ways it performs the same function as Account 100.4, "Telephone plant acquisition adjustment", prescribed in this Commission's system.

The similarity between accounts 100.4 and 278 was recognized by the lower court in its opinion. See quotation on page 51 of this brief and for the same matter see R. 568, last paragraph.

The Uniform System of Accounts under consideration is clearly distinguishable from the system of accounts prescribed by the Public Service Commission in the State of New York, which was held invalid in *New York Edison Company, et al.* v. *Maltbie, et al.*, 244 A. D. (N. Y.) 685, affirmed 271 N. Y. 103.

The difference between (a) the cost to the accounting company of plant acquired from another

public utility and (b) its original cost at time of first dedication to public service (less depreciation applicable at date of acquisition) is, under this Commission's system of accounts, included in *investment* account 100.4, "Telephone plant acquisition adjustment" (R. 123), whereas the system held invalid in the *New York Edison* case required that this residual element be included in a *deferred debit* account styled "143. Suspense to be amortized." See *New York Edison Company* v. *Maltbie, et al.*, 244 A. D. (N. Y.) 685.

Under this Commission's system the residual element included in account 100.4 shall, in accordance with provision (C) under that account, be "disposed of, written off, or provision shall be made for the amortization thereof in such manner as this Commission may direct", depending upon the facts and circumstances surrounding the particular acquisition. Under the New York Public Service Commisison's system, this residual element "shall be written off over such period and in such manner as the Commission [N. Y.] may by order prescribe."

These distinguishing features were clearly recognized by the trial court in its opinion, quoted at p. 51 of this brief; and for the same matter see R. 568, last paragraph, where the court said:

> * * * This flexibility distinguishes the system at bar from that held invalid in New York Edison Co. v. Maltbie (244 A. D. (N. Y.) 685), * * *

See testimony of affiants (1) William J. Norfleet (R. 470–475, figures 1–20, R. 479–480, figures 34, 35, and R. 483, figures 1, 2); (2) Robert S. Rains (R. 486–488, figures 1–8, and R. 491, 492, figure 24); (3) John H. Bickley (R. 504–508, R. 510, letter c, R. 514–516, figures 1–5, R. 517, 518, figures 7 and 8, and R. 519–520, figures 11–15); (4) Asel R. Colbert (R. 525–527); (5) Malcolm F. Orton (R. 534–535, letters A–C, R. 540–542, and R. 543–544); and (6) Charles W. Smith (R. 547–548, letters A–B).

(b) THE ORIGINAL COST PROVISIONS DO *NOT* PREVENT THE APPELLANTS FROM CHARGING ANY DEPRECIATION EXPENSE ON A PART OF THEIR ACTUAL INVESTMENT IN DEPRECIABLE PROPERTY

This subject is related to our proposition II, and is hereinafter discussed thereunder. See p. 42, post.

(c) THE ORIGINAL COST PROVISIONS DO *NOT* REQUIRE, IN EFFECT, A RETROACTIVE CHANGE IN THE ACCOUNTS OF TRANSACTIONS ENTERED INTO BY APPELLANTS, WHETHER WITH OR WITHOUT GOVERNMENTAL APPROVAL

The system of accounts under attack was promulgated June 19, 1935, to become effective on January 1, 1936. It does not, as claimed by appellants, prescribe retroactive changes in the accounts. This is apparent from a reading of paragraph (D) of instruction 2 (R. 97–9) as follows:

> As of the effective date of this system of accounts, the several accounts prescribed herein shall be opened by transferring thereto the balances carried in the accounts previously maintained by the company. Copies of the journal entries recorded to effect these transfers shall be filed with this Commission. The company is authorized to make such subdivisions, reclassifications, or consolidations of such balances as are necessary to meet the requirements of this system of accounts.

This provision was carried over from the "First Revised Issue" promulgated by the Interstate Commerce Commission in 1933, except that the second sentence therein was added by this Commission. This provision does not appear to have been protested by any of the carriers when adopted by the Interstate Commerce Commission. It will be

remembered that it promulgated a system of accounts in 1913, which was revised in 1933. The original system, as well as the revised system, supplanted those which preceded, and were often changed.

The court will find by comparison of the form of balance sheet prescribed by the system under stay (R. 121) with that prescribed by the system now in effect under the stay (R. 376), that investment account 100, "Telephone plant", of the present system (R. 378) is abolished, and that four new investment accounts are prescribed, viz:

100.1 Telephone plant in service.

100.2 Telephone plant under construction.

100.3 Property held for future telephone use.

100.4 Telephone plant acquisition adjustment.

This means that the total amount in account 100 of the present system (R. 378), as of the effective date of the new system of accounts, shall be analyzed and then reclassified in the four new investment accounts as above numbered and named (R. 122–3).

It is evident from the above-mentioned provisions that the Uniform System of Accounts under consideration does not eliminate anything from the carrier's previous records. The new system merely requires, for prospective application and use, classifications different in some respects from classifications in the previous system. Such requirement is authorized under Section 220 (a) of

the Communications Act, and is valid. See *Interstate Commerce Commission* v. *Goodrich Transit Company,* 224 U. S. 194, and *Kansas City Southern Ry. Co.* v. *United States,* 231 U. S. 423.

The Interstate Commerce Commission and the State Commissions have, from the inception of accounting systems regulated by law, required certain classifications of accounts, and classification of items is the fundamental characteristic of the classification of accounts.

See testimony of affiants (1) William J. Norfleet (R. 479, figures 32 and 33); (2) Robert S. Rains (R. 490, figure 16); and (3) Malcolm F. Orton (R. 537, letter H).

(d) THE ORIGINAL COST PROVISIONS ARE *NOT* UNREASONABLY BURDENSOME AND EXPENSIVE, AND THEY *SERVE* A USEFUL PURPOSE IN ADDITION TO THE RECORDING OF INFORMATION WHICH COULD BE MADE AVAILABLE IN SUPPLEMENTARY STATEMENTS PURSUANT TO SECTION 213 (c) OF THE COMMUNICATIONS ACT OF 1934

Burdensomeness and expensiveness of performance under the provisions of the Uniform System of Accounts for Telephone Companies, prescribed by the Federal Communications Commission, are not proper subjects for the consideration of the court. Such questions are within the jurisdiction of the Commission alone. The Commission, however, has not acted arbitrarily, nor unreasonably, in the premises. On this point, see affidavit of Mr. W. J. Norfleet (R. 484).

In *United States, et al.,* v. *Missouri Pac. R. R. Co.,* 278 U. S. 269, 277–8, the court said:

> * * * *Inconvenience or hardships, if any, that result from following the statute as written must be relieved by legislation.* * * * [Italics supplied.]

In the court below, the plaintiffs contested the requirement for keeping a duplicate set of accounts, to some extent, during the first year of the application of the system. The contest on that point, we understand, has been abandoned; and there is here less expensiveness to discuss.

The telephone business has, in some quarters, been estimated to have assets exceeding five billion dollars—an amount said to be about one-fourth the value of all the railroads in the country. It is to be assumed that if there is to be effective regulation of the telephone carriers there necessarily must be reasonable expense therewith associated.

The reason underlying the *original cost* provisions of the Uniform System of Accounts under stay and the purposes served thereby were clearly and concisely stated by Mr. W. J. Norfleet in his affidavit, as follows (R. 470):

> * * * The reason for this requirement is the need for continuity and uniformity in accounting for the original cost regardless of the changes in ownership of the property or the incident of ownership at a given time, and to bring about uniformity in the statement of plant accounts of public utilities. Such continuity and uniformity are essential from the standpoint of charges to operating expenses for depreciation, from the standpoint of passing upon security issues, from the standpoint of considering the reasonableness of the purchase price of property to be acquired, and from the standpoint of valuation for rate-making purposes.

On this subject, Mr. Norfleet further testified as follows (R. 471–2):

> With respect to a minor part of telephone plant now in existence which was acquired

by the telephone company from other public utilities, the telephone companies have indulged in optional accounting with the result that certain property so acquired has been included in the plant accounts at "actual cost to the company", other property being recorded by a "merger of the book accounts", other property being recorded at the "current cost new", and still other property at "structural value."

* * * * *

Although the plant accounts are now stated as heretofore described, depreciation charges are computed on "book cost", and retirements are made on "average cost" or "original cost." The Commission's system of accounts corrects these inconsistencies in addition to providing information for the other purposes hereinbefore mentioned, in that it requires all items of telephone plant account to be stated on basis of "original cost" and that depreciation and retirements be computed on the same basis.

The appellants denounce the application of Section 220 (a) of the Communications Act of 1934 in such way as to require the inclusion in account 100.1 of the item of *original cost* as defined in the Uniform System of Accounts, because, as they say, a statement of such *original cost* may be had under Section 213 (c) of the Act; but, as the trial court said (R. 566):

* * * The powers conferred by Section 213 (c) are not restrictive of Section

220 (a) nor does the latter section restrict the former. The two sections are capable of complementary treatment.

Section 213 (c) provides in part:

> The Commission may at any time require any such carrier to file with the Commission a statement showing the original cost at the time of dedication to the public use of all or of any part of the property owned or used by said carrier. * * *

The gist of the foregoing is that the Federal Communications Commission *may at any time* call for the *statement showing the original cost* therein mentioned.

The mere possibility of performance under provisions above quoted from Section 213 (c) which the Commission may but is not obligated to apply, cannot be invoked by the carriers to defeat performance which the Commission may and does require under Section 220 (a); furthermore, Section 213 (c) assumes—at least contemplates—the possibility of an established system of accounts to which recourse may be had to obtain the *statement* which may be separately required under the aforesaid Section 213 (c), as it continues as follows:

> * * * For the showing of such original cost said property shall be classified, and the original cost shall be defined, in such manner as the Commission may prescribe; and if any part of such cost cannot be determined from accounting or other records,

> the portion of the property for which such cost cannot be determined shall be reported to the Commission; and, if the Commission shall so direct, the original cost thereof shall be estimated in such manner as the Commission may prescribe. * * *

As further indication that Congress did not intend that Section 220 (a) should be subservient to or superseded by Section 213 (c), we notice the following language of the latter section:

> * * * If the carrier owning the property at the time such original cost is reported shall have paid more or less than the original cost to acquire the same, the amount of such cost of acquisition, and any facts which the Commission may require in connection therewith, shall be reported with such original cost. * * *

The said Section 213 (c) further provides:

> * * * The report made by a carrier under this paragraph shall show the source or sources from which the original cost reported was obtained, and such other information as to the manner in which the report was prepared, as the Commission shall require.

By reference to the Communications Act of 1934, it will be seen that Section 213 falls under the subtitle "Valuation of Carrier Property", and no doubt every subdivision of said section from (a) to (h), inclusive, has some proper function to perform; and, with respect to the application of Sec-

tion 220 (a), at the same time we notice *Kansas City Southern Railway Company* v. *United States, et al.*, 231 U. S. 423, 443, as follows:

> * * * And since, * * *, uniformity in accounting is dependent upon the adoption and enforcement of precise classification, the authority to define the terms of the classification necessarily follows. It amounts, after all, to no more than laying down rules of action under which the Commission shall proceed, and leaving it to the Commission to apply those rules to particular situations and circumstances by the establishment and enforcement of administrative regulations.

Section 213 of the Communications Act is practically identical with Section 19 (a) of the Interstate Commerce Act as amended by the Emergency Railway Transportation Act of 1933.

Section 220 of the Communications Act is derived from Section 20 (5) to (8) of the Interstate Commerce Act.

In *Norfolk & Western Railway Co.* v. *United States, et al.*, 287 U. S. 134, 140–1, the court considered Sections 15 (a), 19 (a), and 20 of the Interstate Commerce Act, and allowed each Section full force and effect.

In *United States* v. *Atlanta B. & C. Ry. Co.*, 282 U. S. 522, 529, the court considered Section 20 (1) to (5) and Section 1 (20) of the Interstate Commerce Act, and allowed full force and effect to each.

In each of the cases cited, the Supreme Court sustained the accounting provisions of the law because such provisions appeared to be necessary in the administration of other provisions of the Act. In the aforesaid *Norfolk & Western* case, particularly, the court sustained an accounting order upon the requirement in the valuation section of the Interstate Commerce Act.

Section 220 (a) and (b) should be allowed to operate in aid of each other—in the light of each other, and in conjunction with Section 219 (a) and (b); and Section 220 (a) to (h) should be allowed to operate in the aid of Section 213 (a) to (h); and in connection therewith it should be noticed that the Federal Communications Commission has duties under Section 204 of the Act, and under Section 205 of the Act, which deal with hearings and orders in rate matters. For the aid of Sections 204 and 205, and to enable the Commission to proceed advisedly thereunder, many other sections should have full and complete application and enforcement.

In *United States* v. *Atlanta B. & C. R. Company, supra,* at p. 527, the court, discussing proceedings before the Interstate Commerce Commission, said:

> * * * Its functions are manifold in character. In some matters its duty is merely to investigate and to report facts. See *United States* v. *Los Angeles & Salt Lake R. Co.,* 273 U. S. 299, 310. In others, to make determinations. See *Great North-*

> *ern Ry. Co.* v. *United States,* 277 U. S. 172. In some, it acts in an advisory capacity. Compare *Minneapolis & St. Louis R. Co.* v. *Peoria & Pekin Union Ry. Co.,* 270 U. S. 580, 584–5. In others in a supervisory. * * *

It is beyond question that the *original cost* provisions of the Uniform System of Accounts, prescribed under Section 220 (a) of the Communications Act, serve useful purposes additional to that of any statement that might be required under Section 213 (c) of the Act.

The attention of the court is respectfully called to *Tri-State Telephone & Telegraph Company Proposed Control,* 180 I. C. C. 229, and to *Tri-State Telephone & Telegraph Company Control,* 193 I. C. C. 383.

The said cases comprised a matter where one of the Bell companies sought to acquire a telephone company at a price far in excess of its true value. The application was denied in the first instance, and, thereafter, the company made a proposal to make the purchase for a much smaller amount. The latter application was approved. The Commission stated, 193 I. C. C. 383, 384–5, that:

> This application * * * was denied on the sole ground that the price proposed to be paid was greatly in excess of the equity in the properties represented by the stock and was therefore not in the public interest * * *.

The appellants have complained of the difficulty of showing *original cost,* but eminent authorities are in disagreement with appellants. See "Railroad Finance and Organization", by William Z. Ripley, at pages 347–8:

> "Book value" or cost of property, as we have already seen, seldom represents anything even approximating to the facts. The meagreness of corporate records, either because of carelessness or bad faith, is indeed a severely practical objection; *and yet experience has already shown that original cost can be unearthed.* The most substantial attempt along this line is the inventory made by the Washington Railroad Commission in 1905. The actual investment was found to be obtainable for practically all of the property. * * * [Italics supplied.]

We see no reason why practical and satisfactory results cannot be obtained by an examination of the historical records of properties acquired by purchase, and by engineering and other studies. Difficulties encountered in determining such an important fact as *original cost* of property in public use do not justify continuation of an improper accounting procedure such as that now in effect. Cf. *Sharfman, The Interstate Commerce Commission,* Vol. III–A (1935), pp. 143, et seq.

The recording of items in the accounts, and particularly telephone plant accounts, on basis of estimates, is not an innovation in public utility ac-

counting, or in any accounting procedure for that matter. For example, the accounting regulations heretofore and now in effect governing the recording of telephone plant purchased (instruction 21), and which appellants have elected to use in many instances, provide that (R. 365–6):

> When property in use in telephone service is purchased, * * * there shall be charged as of the date of purchase: (1) To account 211, "Land", *the estimated current value* of the land; (2) to the depreciable plant accounts, the *current cost new* (*estimated if not known*), of the property classable therein; (3) to account 202, "Franchises", *the original cost* of all governmental franchises and similar rights acquired; and (4) to accounts 232, "Station installations", and 233, "Drop and block wires", such proportion of *the estimated current cost new, etc.* [Italics supplied.]

Incidentally, the accounting now performed by appellants for depreciation and for employees' pensions is almost exclusively based on estimates involving highly complicated actuarial computations.

The testimony of the Chief Accountant of the Federal Communications Commission, and of other accountants of experience and repute, shows that the order under attack in this case, and the accounts and instructions covered thereby, can be competently and fairly applied by the appellants, whether as classes or as individuals.

See testimony of affiants, (1) William J. Norfleet (R. 477–479, figures 26–31, and R. 484, figure 1); (2) Robert S. Rains (R. 489–490, figures 12–15); (3) John H. Bickley (R. 510, letter d); (4) Asel R. Colbert (R. 530); and (5) Malcolm F. Orton (R. 535, letter D, and R. 538, letter B.)

II

THE PROVISIONS OF TELEPHONE DIVISION ORDER NO. 7–C (PARAGRAPH (C) OF THE TEXT OF ACCOUNT 100.4, "TELEPHONE PLANT ACQUISITION ADJUSTMENT") THAT (R. 124): "THE AMOUNTS RECORDED IN THIS ACCOUNT WITH RESPECT TO EACH PROPERTY ACQUISITION SHALL BE DISPOSED OF, WRITTEN OFF, OR PROVISION SHALL BE MADE FOR THE AMORTIZATION THEREOF IN SUCH MANNER AS THIS COMMISSION MAY DIRECT" ARE *Not* VOID

The phrase "disposed of" is primarily defined by recognized lexicographers as meaning "arranged or set in order", and not as meaning "extinguished or annihilated" as intimated by appellants. An item in this account may be disposed of by allowing it to rest in the account until the property to which it is related is retired from service.

The points numbered I–b and II in the Statement of Points, upon which appellants rely in their appeal in this case, are so closely related (see p. 27, ante) that we have until now postponed discussion of proposition I–b to avoid repetition (notice, too, discussion of the *New York Edison* case, appearing in this brief, ante p. 24, et seq.).

The provisions of this Commission's system of accounts, now under attack, which would govern appellants' accounting for depreciation, are separate and distinct from the provisions governing the accounting for recording their investment in plant. It is, therefore, apparent that the original cost provisions neither prevent nor require the accounting for depreciation expense by the appellants.

The point which appellants apparently would make by their statement (I–b), is that account 100.4, "Telephone plant acquisition adjustment", in which is included a part of their investment, is not designated a depreciable account *as such* in this Commission's system.

This is not new in accounting, nor unique in the system under attack. There are other means of accounting for loss in service value of property than by charges to operating expenses for depreciation. Appellants are not now permitted, nor have they since 1913 been permitted to include in operating expenses, through charges for depreciation, the full purchase price of property.

Under the present system a part of appellants' investment in plant is now recorded in account 278, "Undistributed cost of property" (R. 404). Depreciation accounting is not permitted for property represented by amounts in this account, and the amounts recorded therein can be (and properly should be) extinguished only through surplus.

A part of appellants' investment is now recorded in accounts 202, "Franchises", and 203, "Patent rights" (R. 394). These investments are not now designated as depreciable, but provision is made for the amortization thereof in such manner as to produce the same result as would obtain under depreciation accounting.

A part of appellants' investment in plant is now recorded in accounts 232, "Station installations", and 233, "Drop and block wires" (R. 399). These properties depreciate just as any other depreciable property, but the accounts in which investment in such property is recorded are not designated as accounts covering classes of depreciable telephone plant (instruction 82, R. 376). Because of circumstances peculiar to such property, the full service loss is charged to operating expenses at time of retirement.

There were sound reasons for the Interstate Commerce Commission's accounting treatment of the foregoing properties, to wit: "Undistributed cost of property", "Franchises", "Patent rights", "Station installations", and "Drop and block wires", and for omitting such properties from the classes of depreciable telephone plant.

The Federal Communications Commission is authorized by Section 220 (b) of the Communications Act of 1934 to:

> * * * prescribe * * * the classes of property for which depreciation charges may be properly included under operating

> expenses, and * * * when it deems necessary, modify the classes * * * so prescribed. * * *

In exercising its authority in this respect, this Commission has prescribed certain classes of telephone plant named in instruction 82 (R. 120). There are sound reasons underlying the omission by this Commission of property represented by account 100.4, "Telephone plant acquisition adjustment" (R. 123), from the classes of depreciable property.

There are also sound reasons underlying provision (C) of the text of account 100.4, "Telephone plant acquisition adjustment", that (R. 124):

> The amounts recorded in this account with respect to each property acquisition shall be disposed of, written off, or provision shall be made for the amortization thereof in such manner as this Commission may direct.

The Commission might have followed the present system, by providing that the amounts recorded in account 100.4 should be extinguished only through surplus, or in the same manner as that part of appellants' investment now recorded in account 278, "Undistributed cost of property" (R. 404), can be disposed of. Such a provision would, in some instances, be unfair to appellants. Provisions might also have been made that all amounts recorded in account 100.4 should be extinguished only through charges to operating ex-

penses for depreciation thereof. Such a provision would be unfair to the subscribers in those instances involving capitalization of earning power, cost of elimination of competition, excessive payments to affiliates, and other costs not in the public interest. Provision might also have been made for distribution of the amounts recorded in account 100.4 equally between operating expenses and surplus, but this provision, or any other such provision, would, under some circumstances, be arbitrary and unreasonable.

In view of the foregoing, the Commission has recognized the necessity of ascertaining facts in each individual case before prescribing the final accounting to be performed in that case. It should be apparent that such provision is imperative in the interest of fairness to all parties and for purposes of maintaining uniformity in accounting procedure.

Furthermore, where the accounts of utilities of different sizes and different business practices and policies are to reflect the purchase of property from predecessor companies, and from affiliated companies, and such acquisitions are frequently made through the purchase or exchange of securities or properties, the issuance of individual orders requiring a particular carrier to make specific entries with respect to transactions as to which no inflexible specific accounting rules, regulations, or classifications can be nicely or precisely made un-

til the facts are known, is proper, orderly, and valid; and it is necessary, if the public regulation of public utilities is to be useful and successful. (See instruction 21 (C) (R. 109).)

As we have previously stated, amounts included in account 100.4, "Telephone plant acquisition adjustment", (R. 123) may represent, under differing circumstances, a portion of the amounts paid for various and sundry tangible and intangible items.

The Uniform System of Accounts contains general rules for the distribution of expenditures, according to their character, to investments, operating expenses, income, surplus, and other accounts. (See instruction 10, "Purpose of balance-sheet accounts" (R. 104); instruction 20, "Purpose of telephone plant accounts" (R. 107); instruction 30, "Purpose of income accounts" (R. 115); instruction 40, "Purpose of surplus accounts" (R. 116); instruction 50, "Purpose of operating revenue accounts" (R. 116); instruction 60, "Purpose of operating expense accounts" (R. 117); and instruction 70, "Purpose of clearing accounts" (R. 118).)

As stated by Mr. W. J. Norfleet in his affidavit (R. 476):

> Affiants for plaintiffs say that the amounts to be recorded in Account 100.4 must be extinguished either immediately or later at the pleasure of the Commission, and

> that such amounts are a deferred charge against surplus, since the Commission can make it such a charge at any time. This is purely speculative and unsupported by the system of accounts, the general rules of which govern the disposition of items not specifically provided for. *The affiants may just as well have made the proper assumption, namely, that the disposition of the amounts to be recorded in Account 100.4, "Telephone plant acquisition adjustment" would be disposed of, after the character of the item had been determined, in a manner consistent with the general rules underlying the uniform system of accounts for the distribution of expenditures, according to their character, to operating expenses, income, surplus, or remain an investment.* [Italics supplied.]

The court below likened amortization to depreciation (R. 569). There is support for such position. See Whitten on "Valuation of Public Service Corporations", 2d ed., section 853, wherein reference is made to the American Telephone and Telegraph Company as recommending the straight line method of depreciation. We quote the following (p. 1830):

> The function of depreciation reserve is to amortize the portion of the expense of conducting the business caused by using up this depreciable property.

The following statements authorized by the Executive Committee of the American Accounting Association appear in an article in the June 1936 issue of "The Accounting Review" (p. 188):

> 5. The application of these principles should be broad enough to cover amortization of fixed assets through allowances for depreciation, depletion, and obsolescence, and reductions of inventory and investment costs to amounts allocable to succeeding periods,
>
> * * * * *
>
> 10. The operations section of the income statement should disclose the gross revenues from sales made and services rendered; the elements of operating cost and expense incurred, including the amount of *depreciation and other amortization* of assets applicable; * * *. [Italics supplied.]

It is apparent from the foregoing that there is abundant authoritative support for treating depreciation as a class or type of amortization. All consumption, in operation, of costs incurred in the acquisition of property in use in telephone service is not necessarily recorded through "depreciation charges." The Commission may rightfully exclude from "depreciation expenses" and style as "amortization expenses", or by any other term found appropriate in the circumstances, amounts appearing in account 100.4 which it finds appellants entitled to recover as operating expenses.

For such recovery the Commission has made among other pertinent provisions the following:

> (1) In provision (B), under account 100.4, the rule that "this account shall be subdivided according to the character of the amounts contained therein" (R. 123);
>
> (2) The statement in instruction 60, that "the operating expense accounts are designed to show the expenses of furnishing telephone service" (R. 117); and
>
> (3) In provision (B), under account 172, "Amortization reserve", the provision that "it shall also be credited with any amounts which this Commission may authorize under a plan to amortize the balance in account 100.4, 'Telephone plant acquisition adjustment'" (R. 140).

Upon comparing the system of accounts under stay during the pendency of this appeal with the system of accounts heretofore and now in effect under the stay, the trial court, upon consideration of the original cost provisions of the new system, entered into a discussion of the objection of appellants that no depreciation is allowed on amounts charged to the "Telephone plant acquisition adjustment" account. Such discussion carries its own argument with it. The court said (R. 568–9):

> On a comparison of the two systems, that of this Commission seems to more accurately reflect the condition and record the history of the plant. Account 100.4 is listed among investments. It can be subdivided

so that there can be segregated any amount therein not representing (1) the cost of elimination of competition; (2) payment to an affiliate at a price in excess of cost to it with a profit returnable to the purchasing company in the form of dividends or otherwise; and (3) any other element not expended in public interest.

This segregated amount would receive the same treatment substantially in the rate and depreciation basis as would amounts appearing in 100.1, "Telephone plant in service." In this light, it appears that the proposed system merely provides segregation, and that the addition of the amounts in these investment accounts 100.1 through 100.4 would accurately picture the legitimate investments of the purchasing company.

To follow the plaintiffs in their argument that a reserve of surplus must be maintained against 100.4 and that this is fundamentally wrong, would be to ignore the similarity between 278 of the present system and 100.4 of the proposed system, and further it requires the assumption that the Commission will act improperly in the future under 100.4 (c). This cannot be presumed. The order provides for alternatives adaptable to the facts of individual cases. This flexibility distinguishes the system at bar from that held invalid in *New York Edison Co.* v. *Maltbie* (244 A. D. (N. Y.) 685). This cannot be held, before any order under 100.4

(c) has been made by the Commission, to be such an arbitrary method of accounting that the order imposing it is void.

The same argument applies to the objection that no depreciation is allowed against item 100.4 "acquisition adjustments." This complaint anticipates arbitrary action by the Commission, under 100.4 (c), which authorizes handling of this item through amortization. The effect would be the same as writing down through depreciation, and until the Commission acts so that the accounts become so contrary to the principles of correct accounting as to constitute the Commission's order arbitrary and unreasonable, the Commission is within its powers. The court need not agree the accounting proposed is the best method, but at this stage it cannot be said the provision is arbitrary. The objection is made that the Commission's refusal to act properly within 100.4 (c) would constitute a negative order, nonreviewable within the doctrine of *Procter & Gamble* v. *United States,* 225 U. S. 282. This would not cut off the plaintiff's right of attacking the system as it would apply to them after such a refusal. The appeal need not be on the order denying relief but can be against the system as its operation is affected by such denial.

There is no deprivation of property involved here. The Supreme Court has noted that the question merely concerned accounting and that there was no occasion to hold

> the order invalid as a deprivation of property until actual damage was threatened by it as in the use of an improper rate base in setting rates. *Norfolk & Western Ry. Co.* v. *United States,* 287 U. S. 134; *United States* v. *Los Angeles & Salt Lake R. R. Co.,* 273 U. S. 299.

In the last paragraph on page 15 of their brief additional appellants state:

> We are discussing the right of the Commission under the guise of prescribing "forms of account" to require these companies to write off from their books a loss which they have in fact not suffered.

This Commission has assumed no such right in the system of accounts under attack in this suit. The Commission has, and we believe rightfully so, reserved the right to require a company to write off from its books a loss *which they have in fact suffered.* This, we believe, is in the public interest *in order that the reader of the balance sheet may be correct in assuming that amounts paid for property which is no longer in existence are not included in the balance sheet as investment in telephone plant. This cannot be correctly assumed under the system heretofore and now in effect.*

There may be instances where the purchase price of property is represented by exorbitant amounts paid for the capital stock of the company whose property is acquired. Under such circumstances it would be fitting and proper that such portion of

that cost as does not represent value received should be written off to surplus. Furthermore, securities of the acquiring company are often exchanged for property, and valuations placed on such securities by the acquiring company may be excessive. Surely such excessive valuations should not be included in depreciable telephone plant accounts or otherwise shown in the balance-sheet statement as legitimate investments.

Under provision (C) stated below account 100.4, "Telephone plant acquisition adjustment" (R. 124), carriers are not compelled—in the light of the alternatives provided therein—to write off any amount in said account.

Provision (C) stated below account 100.4 is a statement directory in character setting forth means further to account for items included in said account and merely provides for alternate actions that may be found appropriate by the Commission in cases arising in the future. Without such future action, there will be no case or controversy subject to judicial review. Until then, said provision (C) will remain purely directory or advisory. Contrast *United States v. Atlanta B. & C. Ry. Co.* (1931), *supra,* with *Atlanta B. & C. Ry. Co.* v. *United States* (1935), 296 U. S. 33, wherein the Supreme Court distinguished between an accounting order which is subject to judicial review and an order, merely declaratory of rules, not subject to review.

All contention respecting the propriety of instructions, as distinguished from the validity of accounts, is therefore prematurely precipitated. The attempt to invalidate instructions or provisions in the nature of directions or instructions in the Uniform System of Accounts, at this time, is based upon no consummate right. It is without present foundation either in fact or law.

As the trial court said, the appellants have been done no actionable wrong until the Federal Communications Commission shall have made some arbitrary and unreasonable requirement with respect to disposition of amounts in investment account 100.4.

See testimony of affiants (1) William J. Norfleet (R. 476–477, figures 21–25, and R. 481–482, figures 1–4); (2) Robert S. Rains (R. 488–489, figures 9–10, and R. 490, figure 17); (3) John H. Bickley (R. 511–512, 516, figure 6, R. 518–519, figures 9–10, and R. 520–521, figures 16–17); (4) Asel R. Colbert (R. 527–528); (5) Malcolm F. Orton (R. 535–537, letters E–G); and (6) Charles W. Smith (R. 548–549, letters C–D, and R. 550).

The District Court did *not* err in holding said provisions valid.

III

Instruction 2 (B.1) of the Order Assailed by the Appellants Is *Not,* In Its Requirement, So Arbitrary and Unreasonable As To Be Beyond the Authority of the Federal Communications Commission to Prescribe, and It Does *Not* Deprive the Appellants of Their Rights Under the Due Process Clause of the Fifth Amendment to the Constitution of the United States

The aforesaid instruction is by its terms expressly applicable to *charges* to certain accounts, to wit: those *prescribed* for Telephone Plant, Income, Operating Revenues, and Operating Expenses. Such charges must be *just and reasonable* and any payments in excess of *just and reasonable charges* must be charged to another account, known as "Miscellaneous income charges" (R 163).

The Federal Communications Commission is authorized by the Communications Act of 1934, Section 220 (a), to prescribe the forms of accounts—to outline the formulas. Whether the method of formulating the accounts is reasonable or unreasonable, and whether the segregation of accounts out of some accounts into other accounts, is proper or improper, are questions of fact. (See *Groesbeck et al.* v. *Duluth, South Shore & Atlantic Rail-*

way Company, 250 U. S. 607; see particularly the concluding part of the opinion, at p. 614.) Questions of fact are for the Commission—not for the court.

The Act to Regulate Commerce (49 U. S. C., Chap. 1; 41 Stat. 474), in numerous sections, and in many ways, engages the phrase *just and reasonable,* and its opposite, *unjust and unreasonable,* to characterize things respectively required or prohibited by said Act. See Sections 1 (4), 1 (5), 1 (6), 1 (8), 1 (11), 1 (12), 1 (15) (b), 1 (16), 1 (17), 1 (21), 3 (1), 3 (4), 4, 5 (1), 5 (2), 10 (4), 15 (1), 15 (6), 15 (7). As illustrative of such use of said expressions, we notice Section 1 (5), as follows:

> All charges made for any service rendered or to be rendered in the transportation of passengers or property or in the transmission of intelligence by wire or wireless as aforesaid, or in connection therewith, shall be *just and reasonable,* and every *unjust and unreasonable* charge for such service or any part thereof is prohibited and declared to be unlawful. [Italics supplied.]

In the matter of the Investigation and Suspension of Advances in rates for the transportation of coal by the Chesapeake and Ohio Railway Company and other carriers, XXII I. C. C. 604, the justice and reasonableness of the rates was the sole question involved. On page 624 the Commission said:

> * * * The words "just and reasonsonable" imply the application of good

> judgment and fairness, of common sense and a sense of justice to a given condition of facts. * * *
>
> * * * A just and reasonable rate must be one which respects alike the carriers' deserts and the character of the traffic. * * *
>
> * * * There is, however, a zone within which we may properly exercise "the flexible limit of judgment which belongs to the power to fix rates." These are the words of the Chief Justice of the Supreme Court, 206 U. S. 26. * * *

Other cases on this subject to which the attention of the court is directed are *Pennsylvania Co.* v. *United States,* 236 U. S. 331, 361, and cases cited; *Interstate Commerce Commission* v. *Alabama Midland Ry. Co.,* 168 U. S. 144, and cases cited; *Philadelphia & R. Ry. Co. et al.* v. *Interstate Commerce Commission,* 174 Fed. 687, 688; *Pennsylvania Railroad Company* v. *International Coal Mining Company,* 230 U. S. 184; *Standard Oil Company* v. *United States,* 221 U. S. 1; and *United States* v. *American Tobacco Company,* 221 U. S. 106.

The foregoing citations are ample to show that the idea of "just and reasonable" is old in public utility regulation. The gist of appellants' argument at pages 36 to 38 of their brief appears to be: (1) that instruction 2 (B. 1) requires the accounts to record what in someone's judgment should have been spent rather than what was spent;

(2) that since net operating income is one of the most vital items in the company's statements, outlays of money, being paid and non-recoverable, should enter into the computation of net operating income irrespective of whether or not they are reasonable or unreasonable, and (3) that, under the instruction, the accounting company acts at the peril of criminal prosecution in recording every item of outlay for property, wages, salaries, or other expenses.

With respect to the first contention, it should be noted that under instruction 2 (A) of the Uniform System of Accounts (R. 97), the appellants are required to keep records of sufficient particularity to show fully all the facts pertaining to all entries in the aforesaid Uniform System of Accounts. The sources of charges to Telephone Plant, Income, Operating Revenues and Operating Expenses under instruction 2 (B. 1) are found in the records to be kept under instruction 2 (A).

Instruction 2 (B. 1) does not impose upon appellants any incorrect or unsound method for making charges to accounts mentioned therein, nor does it postulate obedience to any indefinite or vague standard of conduct contemplated thereby.

Instruction 2 (B.1) deals primarily with charges, merely directing that they, to wit, charges, "shall be just and 'reasonable'," and secondarily with "payments by the company in excess of such just and reasonable charges." The instruction shows no intent to determine what payments shall be

made. It only deals with charges after payments are made.

Although it may be the duty of a bookkeeper to make entries in accordance with transactions, the officers and managers of a public utility have some responsibility to the public as well as to the company, and it is their duty under the law to see that all transactions are just and reasonable, not only to the company, but to the public.

While there may be a presumption that all transactions entered into by and between a public utility and another are reasonable and just, and while it may be that responsible accounting officers should record transactions as they occur, in this connection it must not be overlooked that, when accounting is made and reported, the Commission has a right to reject the accounting as made and to require something in lieu thereof. That, perhaps, is the reason why, in Section 220 (g) of the Act, reference is made to "keeping of accounts, records, and memoranda" prescribed, and then further reference is made to such accounts, records, and memoranda "as may be approved by the Commission." Upon the rejection of any report covering an account which the accounting officers considered prima facie to be just and reasonable, the Commission, under Section 220 (d) of the Act, would have a right to direct that the excess above just and reasonable charges should be charged to account 323, "Miscellaneous

"income charges" (R. 163); and it affords the Commission a better basis for requiring such transfer to have the specific demand in the first instance that all charges be just and reasonable.

In view of the foregoing, we see no merit in the second contention of appellants.

The appellants' third contention is hereinafter discussed at pages 63–66.

103991—36——5

(a) THE INSTRUCTION IS *NOT* CONTRARY TO THE FUNDAMENTAL PRINCIPLES OF CORRECT ACCOUNTING, AND IT WOULD *NOT* COMPEL A FALSIFICATION OF THE ACCOUNTS OF THE APPELLANTS

This statement is fully covered in the discussion of other propositions herein argued (see pp. 56–61 ante), and in addition thereto we bring to the attention of the court the following statement of Mr. W. J. Norfleet in his affidavit (R. 484):

> In my opinion and for the reasons heretofore mentioned, the requirements of this Commission's system of accounts are in no way contrary to fundamental principles of correct accounting but are, in fact, in conformity therewith and are neither arbitrary nor unreasonable.

See testimony of affiants (1) William J. Norfleet (R. 482–483, figures 1–2); (2) John H. Bickley (R. 513–514, and R. 522, figure 27); (3) Asel R. Colbert (R. 529); (4) Malcolm F. Orton (R. 539–540); and (5) Charles W. Smith (R. 551).

(b) THE INSTRUCTION DOES *NOT* LAY DOWN A RULE OF ACCOUNTING, TO WHICH APPELLANTS MUST CONFORM ON PAIN OF THE STATUTORY PENALTIES, SO VAGUE AND INDEFINITE AS NOT TO CONSTITUTE A LEGAL STANDARD OF CONDUCT

The decisions heretofore cited and previous comment abundantly refute appellants' contention that the aforesaid instruction lays down a rule of accounting so vague and indefinite as not to constitute a legal standard of conduct.

In support of their third contention (ante p. 59) that, under the aforesaid instruction, the accounting company must act at the peril of criminal prosecution in recording every item of outlay, appellants cite the following cases:

United States v. *Cohen Grocery Co.*, 255 U. S. 81;

Tedrow v. *Lewis & Son Co.*, 255 U. S. 98;

Small Co. v. *American Sugar Refining Co.*, 267 U. S. 233;

Connally v. *General Construction Co.*, 269 U. S. 385;

Cline v. *Frink Dairy Co.*, 274 U. S. 445.

None of the foregoing cases is applicable to the suit at bar.

In the first three cases cited, the Lever Act, which made it an offense against the United States, punishable by fine or imprisonment, "to make an

unjust or unreasonable rate or charge in handling or dealing in or with any necessaries", was under attack.

The fourth case cited involved a state law which made it a crime to pay, "less than the current rate of per diem wages in the locality in which the work was performed."

In the fifth case cited, the court examined a state law which covered different sorts of conspiracies and combinations in restraint of trade, employing terms which the court said, "sufficiently describes for purposes of a criminal statute the acts which it intends to punish" (pp. 455–6).

Congress has the power to delegate to the Federal Communications Commission the authority to prescribe the uniform systems of accounts and the exercise of that power is not an unlawful delegation of the legislative function. See *Interstate Commerce Commission* v. *Goodrich Transit Company, supra,* at pp. 214–5; *Kansas City So. Ry.* v. *United States,* 231 U. S. 423, 443.

The Communications Act of 1934, like the Interstate Commerce Act, created a commission as a legislative agency authorized to determine what is reasonable or unreasonable with respect to the regulation of carriers; and a carrier subject to the regulation of the Federal Communications Commission may and can, in every instance, know in advance what is required in any case long before criminal prosecution may or can be lodged in any court.

Section 220 (a) of the Communications Act of 1934 is derived from Section 20 (5) of the Interstate Commerce Act and the Supreme Court, referring to that section in *Kansas City So. Ry. Co.* v. *United States,* 231 U. S. 423, 443, said:

> * * * it amounts after all to no more than laying down the general rules of action under which the Commission shall proceed, and leaving it to the Commission to apply those rules to particular situations and circumstances by the establishment and enforcement of administrative regulations.

The proposition that instruction 2 (B. 1) is arbitrary and void under the *due process clause* is untenable. That is certain which is capable of being rendered certain.

Instruction 9 of the Uniform System of Accounts provides (R. 104):

> To the end that uniformity of accounting may be maintained, the company shall submit all questions of doubtful interpretation of the prescribed accounting to this Commission for consideration and decision.

See also Section 220 (g) of the Communications Act of 1934, under which the Commission may approve accounts with the same authority as it prescribes them under Section 220 (a).

The trial court, discussing instruction 2 (B. 1), in its opinion, said:

> The information this requirement makes available is essential to any determination

> of reasonable rates within 201 (b) of the Act * * * (R. 570).
>
> * * * telephone companies need incur no risk since those occasional cases which may be doubtful can be submitted for approval under Sec. 220 (g) of the act and instruction 9 of the order * * * (R. 571).
>
> The necessity of this order becomes apparent upon consideration of the interrelations of telephone companies. License agreements between subsidiaries can furnish examples of charges clearly not "just and reasonable." Yet any exact definition would be objectionable as arbitrary (R. 571).

The District Court did *not* err in holding said instruction valid.

IV

ORDER NO. 7–C OF THE TELEPHONE DIVISION OF THE FEDERAL COMMUNICATIONS COMMISSION DOES *Not*, WITH RESPECT TO INVESTMENTS IN ITEMS OF PROPERTY TO BE ENTERED RESPECTIVELY IN ACCOUNTS 100.1, 100.3, AND 103, LAY DOWN RULES OF ACCOUNTING SO VAGUE AND INDEFINITE AS NOT TO CONSTITUTE A LEGAL STANDARD OF CONDUCT UNDER APPLICABLE PROVISIONS OF LAW, AND THE REFERABLE INSTRUCTIONS IN SAID ORDER ARE *Not* ARBITRARY, AND THEY DO *Not* DEPRIVE THE APPELLANTS OF THEIR RIGHTS UNDER THE DUE PROCESS CLAUSE OF THE FIFTH AMENDMENT TO THE CONSTITUTION OF THE UNITED STATES

The provisions of the system of accounts complained of by the appellants, whether directly or indirectly, are as follows:

> 100.1. *Telephone plant in service.*—This account shall include the original cost (note instruction 3–S.1) of the company's property used in telephone service at the date of the balance-sheet as classified under accounts 201 to 277, inclusive. (Note also instructions 3–AA, 20, and 21.) (R. 122–3.)
>
> 100.3. *Property held for future telephone use.*—(A) This account shall include the original cost (note instruction 3–S.1) of

property owned and held for imminent use in telephone service under a definite plan for such use.

(B) The property included in this account shall be classified according to the primary accounts for telephone plant in service. Separate subaccounts shall be provided for this purpose which accounts shall carry the same numbers as the plant accounts except that each account shall be prefixed by (1). (Note also instructions 20 and 21.) (R. 123.)

103. *Miscellaneous physical property.*—This account shall include the company's investment in physical property other than property the investment in which is includible in accounts 100.1, "Telephone plant in service", 100.2, "Telephone plant under construction", and 100.3, "Property held for future telephone use." It shall include the company's investment in telephone property retired (note instruction 3–T) and held for sale; also property such as lighting, water, power, and manufacturing plants, not held incident to the company's telephone operations, and assessments against miscellaneous physical property for the construction of public improvements (R. 125).

3. *Definitions.*—When used in this system of accounts:

* * * * *

(O) "Miscellaneous physical property" means all physical property owned by the company, other than telephone property the

investment in which is includible in accounts 100.1, "Telephone plant in service", 100.2, "Telephone plant under construction", and 100.3, "Property held for future telephone use."

* * * * *

(BB) "Telephone plant" means physical property used in telephone service (R. 99–102).

Argument of appellants and additional appellants, under this point upon which they rely, goes primarily to the use of the word "imminent" in the text of account 100.3 (quoted above) and to the classification of "spare plant."

Unless the use of property in telephone service is "imminent", as that word is used and understood by public utility accountants and regulatory authorities, charges for depreciation, taxes, and maintenance applicable to such property should not be included in net operating income nor should the original cost of the property be included in account 100.3.

The word "imminent" and the term "imminence of use", and what is meant thereby in the public utility field, appear repeatedly in decisions of the Interstate Commerce Commission. See "Statement of Methods", *Texas Midland* case, 75 I. C. C. 1, 162. See also *Chicago, B. & Q. R. Co.*, 134 I. C. C. 1, 38; *Virginian Ry. Co.*, 141 I. C. C. 595, 634; *Chicago and I. W. R.*, 149 I. C. C. 219, 225; *Pennsylvania R. Co.*, 22 Val. Rep. 1, 119; *Pitts-*

burgh C. C. & St. L. Ry. Co., 24 Val. Rep. 1, 54; *New York Central R. Co.*, 27 Val. Rep. 1, 48.

With respect to spare plant, appellants allege at pages 44 to 48 of their brief that the system is vague as to property to be classified under account 100.1, "Telephone plant in service", and then cite instances of switchboards consisting of large sections some of which often are unused; underground conduit consisting of a number of ducts only a part of which initially contain cables; the cables themselves consisting of many pairs of fine wires some of which are spares; and buildings initially containing vacant floor space. Appellants also criticise the statement of the Commission's Chief Accountant in his affidavit (R. 481) that only necessary spare plant is to be included in account 100.1.

It appears that the word "used", as ordinarily applied in public utility accounting is so universally understood that no justification exists for the narrow interpretation which appellants choose to place on the language of the texts of the accounts of this Commission's system, or of the broad unlimited interpretation which they themselves would make.

The classification of spare plant, under this Commission's system, was discussed by representatives of the Federal Communications Commission and of the carriers at a conference held on May 16, 1935, preliminary to promulgating Telephone Division Order No. 7–C. The Commission's interpretation of the provisions of the

Uniform System of Accounts relating to the classification of spare plant, explained to the carriers at that conference, was expressed in the affidavit of Mr. W. J. Norfleet, in the following language (R. 481):

> It is my opinion and understanding that this Commission's system of accounts permits the recording of necessary "stand-by" plant in Account 100.1, "Telephone plant in service" and that periodical transfers between said Account 100.1 and Account 100.3, "Property held for future telephone use" will not be required by reason of seasonable changes or fluctuating demands for plaintiffs' services. It is also my understanding that such interpretation was discussed and made clear at the conference between representatives of this Commission and representatives of plaintiffs and other telephone companies relating to the then proposed system of accounts for telephone companies, on May 16, 1935.

Both appellants and additional appellants must be aware that regulatory bodies rarely question the distinctions made by carriers between items entered in accounts such as 100.1, 100.3, and 103 until they have occasion to inspect the carrier's books of account and underlying data and that it is customary to accept reasonable efforts of corporate officials toward differentiation under a broad rule that has been promulgated where a rigid rule is not feasible. In the *Texas Midland*

case, previously referred to (75 I. C. C. 1, 162), the Interstate Commerce Commission, in discussing the "imminence-of-use rule", said:

> * * * If the carrier asserts that the lands were purchased in good faith, believing that they would be required for carrier purposes, the presumption will be in favor of the carrier, but nevertheless the carrier must be prepared to state the reason upon which its belief is founded and if the reason is found untenable the land is classified as noncarrier. Again * * * The judgment of the carrier is usually accepted. * * *.

There is in the Uniform System of Accounts nothing arbitrary, indefinite, unnecessary, or vague. Order No. 7–C under attack is, under the rule of statutory construction, to be sustained in all of its parts when the language of any account or instruction is alleged to be subject to different interpretations, one of which would make the account or instruction invalid and the other of which would sustain it. See *Arkansas Natural Gas Company* v. *Arkansas Railroad Commission,* 261 U. S. 379, 383–4; *New York C. & H. R. Co.* v. *United States,* 212 U. S. 481; *Knights Templars' and Masons' Life Indemnity Company* v. *Jarman,* 187 U. S. 197; *Houston & T. C. R. Co.* v. *Texas,* 177 U. S. 66.

See testimony of affiants (1) William J. Norfleet, (R. 480–481, figures 1–6); (2) Robert S. Rains,

(R. 491, figures 20–22); (3) John H. Bickley, (R. 508–510, and R. 521–522, figures 18–21); (4) Asel R. Colbert, (R. 528–529); and (5) Malcolm F. Orton, (R. 537–538, and R. 538, letter A.).

The District Court did *not* err in holding said provisions valid.

V

The Provisions of Order No. 7–C of the Telephone Division of the Federal Communications Comission, Challenged by the Appellants, *are* Separable from the Other Provisions of the Order, and the Order, as a Whole, Is *Not* Void Because of Any Illegality of Any of Its Provisions

The court below held (R. 581–2) that the failure of Telephone Division Order No. 7–C to make specific provision for depreciation of the classes of depreciable property, the *original cost* of which is included in account 100.3, "Property held for future telephone use", was unjustifiable; and condemned the provisions of paragraph (3) of provision (B), under instruction 21 (R. 108–9), relating to the accounting for contributions made to predecessor utilities for construction and acquisition of telephone plant subsequently acquired by appellants.

With respect to accounting requirement for depreciation of property held for future use, it is the duty of the Commission alone to supply the remedy for the discrepancy if there be anything lacking under the ruling of the court.

Instruction 21 (B) (3), condemned by the trial court, can be lifted bodily from the system and the completeness of the system will remain unimpaired.

Section 220 (a) of the Communications Act of 1934 covers accounts, records, and memoranda;

and the system under consideration extends to "original entries" or to books "of evidential character", as did the system upheld in the *Kansas City Southern* case, *supra,* and the system requires the carriers to keep records of particulars and books of general entries. (See instruction 2 (R. 97).) Surely such provisions should not be annulled.

The Uniform System of Accounts contains many accounts and instructions preceding the accounts and appearing as directions under the accounts, as, for instance, provisions (B) and (C), stated under account 100.4, "Telephone plant acquisition adjustment" (R. 123–4), and (B), stated under account 100.3, "Property held for future telephone use" (R. 123). Many of the instructions passed unattacked in the suit.

Under the law, the Federal Communications Commission itself is empowered to construe and apply its system of accounts, but if the court exercises jurisdiction invoked for the suppression of any of the accounts prescribed by the system, then the court no doubt will look to the provisions of the system, which are in writing, to determine what each provision means and what the relation of any provision is to all other provisions of the system. If the question of the separability of the system of accounts is a mixed question of law and fact, then it should be noticed that, as said in *West Ohio Gas Co.* v. *Public Utilities Commission of Ohio,* 294 U. S. 63, 70, "this court does not sit as a board of revision with power to review the action of admin-

istrative agencies upon grounds unrelated to the maintenance of constitutional immunities"; and it should also be noticed that the Commission's affiants testified that the system is separable. See affidavits of Messrs. Norfleet (R. 483–484, VII), Rains (R. 492, figure 25), and Orton (R. 542. figure 8).

Neither the law controlling different coordinate branches of government nor that comity which ought to and does exist between the branches of government countenances the suggestion of appellants that because of their attack upon a few provisions of the accounting system the entire system should be enjoined, set aside, annulled, suspended, and thus wholly obliterated.

The District Court did *not* err in holding such provisions to be separable.

CONCLUSION

The presumption is that the decision of the trial court is correct on the Statement of Points (R. 600); and the burden is on the appellants to sustain their points. That burden has not been discharged either in part or in whole; and the decision of the trial court should be affirmed.

Respectfully submitted,

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Assistant Counsel.

U. S. GOVERNMENT PRINTING OFFICE: 1936

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No. 74

In the Supreme Court of the United States

OCTOBER TERM, 1936

AMERICAN TELEPHONE & TELEGRAPH COMPANY ET AL., APPELLANTS

v.

UNITED STATES OF AMERICA, FEDERAL COMMUNICATIONS COMMISSION ET AL., RESPONDENTS

BRIEF ON BEHALF OF THE NATIONAL ASSOCIATION OF RAILROAD AND UTILITIES COMMISSIONERS

CLYDE S. BAILEY,
JOHN E. BENTON,
Counsel for said Association.

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Argument—Continued. Page

IX. The provisions of Order No. 7-C challenged by the appellants are severable from the other provisions of said order, and the validity of the order, as a whole, does not depend upon the validity of those provisions 100

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BRIEF ON BEHALF OF THE NATIONAL ASSOCIATION OF RAILROAD AND UTILITIES COMMISSIONERS

OPINION BELOW

The opinion of the District Court (R. 561) is reported in 14 Fed. Supp. 121.

STATEMENT OF THE CASE

This is an appeal from the final decree of a specially constituted District Court for the Southern District of New York entered in a suit brought to enjoin enforcement of an order of the Federal Communications Commission prescribing a uniform system of accounts for telephone companies.

The action was instituted by the American Telephone and Telegraph Company and twenty-eight

of its principal subsidiaries (R. 1). Additional groups of telephone companies later appeared as additional plaintiffs (R. 222–237) or as intervening plaintiffs (R. 241–250).

The National Association of Railroad and Utilities Commissioners, described as "a voluntary Association, including in its membership the members of the railroad commissions, public service commissions, and other regulatory commissions and boards of the several States of the United States, except the States of Delaware and New York", filed a petition for leave to intervene as a party defendant, setting forth the part which had been taken by the State commissions, represented in the membership of said Association, in favoring the adoption of said order of the Federal Communications Commission, and their interest therein; and said Association was duly admitted as an intervening defendant (R. 266–271).

Said order of the Federal Communications Commission was designated as "Telephone Division Order No. 7–C." It was issued on June 19, 1935, to become effective January 1, 1936 (R. 91–92).

The District Court, after a hearing and after submission of the case for a final decree, granted a temporary stay of said order No. 7–C pending decision on the motion for an interlocutory injunction (R. 559–560); but the final decree of that court dissolved such temporary stay, and sustained said Order No. 7–C except with respect to two minor matters concerning which no appeal has been

claimed by any defendant. Enforcement of the order in those two respects was permanently enjoined (R. 584–586).

The accounting system for telephone companies, now in force, was prescribed by the Interstate Commerce Commission effective January 1, 1933 (R. 344 and 345). Upon objection of sixteen State commissions and of the Public Utilities Commission of the District of Columbia, the Interstate Commerce Commission took under advisement suggested changes in this 1933 system (R. 16). A hearing in the nature of argument was held (R. 15) before a single Commissioner, who had been given administrative charge of the proceeding, and the matter was submitted to the Commission without brief (R. 14). This submission was on June 15, 1933, but consideration was delayed because the Commissioner in charge was engaged upon other official duties (R. 14). Finally, on July 9, 1934, after the Federal Communications Commission had been appointed, but before it had organized, the Interstate Commerce Commission issued a report, without an order, as was stated by the Interstate Commerce Commission in the report, "in order that it (the new Commission) may be advised of our views" (R. 14). In this report some of the matters now objected to by the appellants were discussed and disapproved (R. 13–82).

Following its organization, the Federal Communications Commission, after an investigation and after conferences both with representatives of

the telephone companies and of the State commissions, adopted said Order No. 7–C revising the outstanding system of accounts for telephone companies. In such revision the accounting representatives of the State commissions in said conference concurred (R. 270).

The National Association of Railroad and Utilities Commissioners, at its convention following such adoption, by resolution, endorsed the system of accounts as promulgated in said Order No. 7–C and recommended its adoption by all State commissions having jurisdiction over telephone companies (R. 268–270).

Numerous grounds of invalidity of this order were asserted in the appellants' bill of complaint; but the matters relied upon in this court, and covered by their "Statement of Points" (R. 600–605) are the following:

(1) Said Order No. 7–C contains provisions which require that the accounts of each company accounting thereunder shall be kept in such form that the original cost of property to a public utility which first dedicated such property to public use shall be shown either in Account "100.1, Telephone Plant in Service", "100.2, Telephone Plant Under Construction", or "100.3 Property Held for Future Telephone Use", and any excess above such original cost which the accounting company may have paid in acquisition thereof in another account, "100.4, Telephone Plant Acquisition Adjustment" (R. 122–124).

"Original cost" is defined as "the actual money cost of (or the current money value of any consideration other than money exchanged for) property at the time when it was first dedicated to the public use, whether by the accounting company or by a predecessor public utility" (R. 101, S. 1).

If the original cost required to be recorded is not known, said Order No. 7–C requires that it shall be estimated (R. 108). It is further provided that the amounts recorded in said account 100.4, with respect to each property acquisition, "shall be disposed of, written off, or provision shall be made for the amortization thereof in such manner as the Commission may direct" (R. 124).

It is claimed by the plaintiffs, that these provisions are so arbitrary and unreasonable as to be beyond the authority of the Commission to prescribe, and that they deprive the appellants of their property, and of the right to keep a reasonable set of accounts, in violation of the Fifth Amendment to the Constitution of the United States (R. 600–601).

(2) The appellants also claim that the provision that the difference between the cost of property to the accounting company and the cost to the public utility which first dedicated such property to public use "shall be disposed of, written off, or amortized as the Commission may direct" is void, for the reason, as the appellants claim, that the Commission's power is limited to the making of rules and regulations of general application, and does not

extend to the making of orders of the character contemplated by the quoted provision (R. 601).

(3) The accounting order also provides:

> (B. 1) All charges to the accounts prescribed in this classification for telephone plant, income, operating revenues, and operating expenses shall be just and reasonable, and any payments by the company in excess of such just and reasonable charges shall be included in account 323, "Miscellaneous income charges" (R. 98).

The appellants contend that this requirement is so arbitrary and unreasonable as to be beyond the authority of the Commission, and that it deprives the appellants of their rights under the due process clause of the Fifth amendment of the Constitution of the United States (R. 602).

(4) Said order further requires that the property of an accounting company shall be classified, and that the original cost of property "used in telephone service at the date of the balance sheet" shall be kept in account 100.1, that the original cost of property "not completed, ready for service at the date of the balance sheet" shall be included in said account 100.2, and that the original cost of property "held for imminent use in telephone service under a definite plan for such use" shall be kept in account 100.3 (R. 122–123).

The appellants claim that the instructions contained in the order with respect to what property

shall be entered in each of said accounts are "so vague and indefinite as not to constitute a legal standard of conduct, and that they are accordingly arbitrary and violative of the due process clause of the Fifth Amendment of the Constitution of the United States (R. 603).

(5) These challenged provisions of Order No. 7–C are claimed to be non-severable, and the entire order void by reason of the invalidity of those provisions.

SUMMARY OF ARGUMENT

I

The "original cost" provisions of Order No. 7–C are not in violation of the due process clause of the fifth amendment of the Constitution.

In determining the extent of the power of Congress to regulate the accounts of telephone companies and in construing the act under which such power has been delegated to the Commission, the legitimate purposes for which such power is to be exercised will be taken into account. Accounts of public utilities serve various well recognized purposes which it will be assumed Congress meant to promote, and especially the purpose of rate regulation mentioned in Section 1 of the Communications Act as one of the purposes for which the Commission was created.

The duties of a commission such as the Federal Communications Commission extend far beyond the decision of cases presented to it by complaint. It has the affirmative duty to determine whether rate increases proposed by utilities shall be permitted to take effect without suspension and investigation, and likewise the continuing duty to consider whether the rates of each utility, subject to its jurisdiction, as to which no complaint has been made, are such rates as require no formal investigation by the Commission, or should be made the subject of such investigation. It is impossible for the Commission to perform these duties effectively, as to the great number of utilities subject to its jurisdiction, unless the accounts of such utilities classify, segregate and set forth the facts respecting their property and operations from which conclusions may be drawn as to fair value, and as to operating cost and operating income; and these facts must be so shown that they may be quickly seen and considered.

Accounting systems now in effect fall far short of meeting the needs of regulatory commissions. Rate proceedings are notoriously prolonged, due largely to the delays incident to accounting investigations which are now necessary to obtain from the accounts, or from other sources, information which ought to be carried upon the face of the accounts. The uniform system of accounts, prescribed by Order No. 7–C represents an earnest at-

tempt on the part of the regulatory commissions of the country, both Federal and State, to improve the instrumentalities with which they work, so that they may perform their duties intelligently and with reasonable expedition.

II

The "original cost" provisions of the order do not require appellants to keep their property investment accounts so as to misrepresent their investment in property.

Order No. 7–C does not require that any part of the cost of its property be obliterated from the accounts of any utility, but merely requires a classification of such property and a segregation of original cost, as defined, from additions thereto which may have been included in the price paid for such property upon purchase of the same by one utility from another, after its dedication to public use. The accounts in which original cost is recorded, and Account 100.4, in which excess of purchase price above such original cost is recorded, taken together, will show the full purchase price of property to the accounting company; and will continue to show such full cost unless and until the amounts recorded in Account 100.4 shall be in whole or in part required to be written off by some subsequent order of the Commission.

The fact that after an item, now to be recorded in Account 100.4, under the provisions of Order No.

7–C, shall have been written off, the accounts will thereafter no longer show the full purchase price is no ground of invalidity. The right of an appellant to carry in its asset accounts any aggregate amount as a statement of assets value depends upon whether it in fact holds assets which that amount fairly represents. Order No. 7–C requires only that amounts in excess of original cost which a utility may have paid upon acquisition of property shall be recorded in Account 100.4, and subjected to the scrutiny of the Commission.

A utility can not hereafter be required to write off all or any part of any item recorded in that account unless the facts justify such order. If the facts justify the retention of the item, in whole or in part, as a true statement of asset value, it will then remain, to the extent justified; but if the facts justify an order requiring it to be written off it will properly disappear from the statement of property value made by the company's accounts.

Order No. 7–C is in direct contrast to the order of the New York Commission as construed by the New York courts in *New York Edison Company* v. *Maltbie,* 244 App. Div. N. Y. 685, in that every item recorded in Account 100.4, under the New York order, was required to be written off without regard to the particular surrounding facts, whereas Order No. 7–C leaves the items recorded in Account 100.4 to be hereafter dealt with upon the basis of the facts of each particular case.

III

The "original cost" provisions of the order do not "prevent appellants from charging any depreciation expense on a part of their actual investment in depreciable property."

It is not true that no depreciation may be charged against the amounts recorded in Account 100.4. It is true that no depreciation on such amounts may be charged without permission from the Commission, and that when charged it will be denominated "amortization" and recorded in Account 613 instead of Account 608. To the extent that the facts of any case justify the amortization of any item in Account 100.4 by charges to operating expense, as for depreciation, such charges will be allowed, but to that extent only.

This limitation upon the appellants in the matter of charges for depreciation is probably the gravest objection to the order from their point of view, but it constitutes one of the most necessary provisions of the order for the promotion of the essential purposes of the Communications Act. The point at issue is plain. Order No. 7–C permits all companies to make charges to operating expense, without further order of the Commission, for depreciation of their depreciable property computed upon the basis of the cost of that property when it was first dedicated to public use, but forbids further charges without permission of the Commission, to be obtained upon a showing that the facts justify further charges.

A public utility has no constitutional right to compute and record depreciation charges upon the entire amount which it may have paid for depreciable property, regardless of the relationship between seller and purchaser and of the actual value of the property purchased. Such a claim is negatived by *United Railways* v. *West,* 280 U. S. 234. The true purpose of depreciation accounting is succintly set forth in *Lindheimer* v. *Illinois Bell Telephone Company,* 292 U. S. 150.

The assertion that Order No. 7–C prevents claiming depreciation upon amounts recorded in Account 100.4 assumes arbitrary action hereafter upon the part of the Communications Commission. Such assumption will not be entertained by the court, and, furthermore, is inconsistent with the Commission's purpose, as testified to by its Chief Accountant, and is contrary to finding VIII of the court below.

IV

The "original cost" provisions of Order No. 7–C do not "require a retroactive change in the accounts of utilities subject thereto."

V

The "original cost" provisions of order No. 7–C are not "unreasonably burdensome and expensive", and they will serve important purposes that can not be equally well otherwise served.

Original cost is a relevant factor in the determination of value which has been repeatedly recog-

nized by this court. Congress has recognized its importance, and has expressly authorized the Commission to require any company subject to the Communications Act to report as to its property "the original cost at the time of dedication to public use", to be ascertained from the accounting records or estimated.

The purposes to be served by showing such cost upon the face of the accounts, in the manner provided by Order No. 7–C are such as to make the Commission's order fairly and reasonably within the grant of power from Congress.

The appellants have greatly exaggerated the difficulty and cost of complying with the order. Whatever cost will be involved will be principally incident to the ascertainment or estimation of original cost, and that expense has been expressly sanctioned by Congress.

So long as the Commission acts within the grant of power conferred by Congress, its orders are not subject to judicial review.

VI

The provision of the Commission's order that the amounts recorded in Account 100.4 "shall be disposed of, written off, or provision shall be made for the amortization thereof in such manner as this commission may direct" is not a requirement which exceeds the power of the Commission.

Various considerations move purchasing utilities to pay prices in excess of original cost. Some of these have no relation to value, and some of them are proper to be taken into account in fixing the base upon which to compute rates and annual depreciation charges. In order that the Commission may properly exercise its functions, the accounts of utilities must be so kept that they will show upon their face amounts which should be taken into consideration as representing value for said purposes. They will show this only if the amounts recorded in Account 100.4, which utilities pay upon transfers among themselves in excess of original cost, are eliminated from the accounts insofar as they do not represent asset value. No general order can be framed to provide for such elimination, the necessity for which must be determined upon the facts peculiar to each case.

The Commission's power is adequate. In addition to the general grant of power to prescribe accounts, contained in Section 220 (a), the Commission under Section 4 (i) has power to make any order not inconsistent with the Act which may be necessary in the exercise of its functions.

The appellants are contending for, as an alleged constitutional right, the privilege of overstating their property accounts, and of charging to operating expenses depreciation computed upon such overstated accounts. It is common knowledge that in recent years great numbers of consolidations of utility properties have been made for the purpose

of securing profits from the distribution of an increased volume of securities. The device of the holding company has facilitated the transfer of titles to operating properties at prices bearing no real relation to value.

If regulatory commissions are to exercise their functions effectively they must have power to examine into statements of cost, and to require such changes in accounts to be made as may be necessary to cause them to state the facts which they purport to state, and in a manner uniform for all companies. Under Order No. 7–C the accounts of all utilities subject to the Commission will show the cost of their operating property upon a uniform basis—that of original cost—and will show also, in Account 100.4, whatever amounts additional thereto paid by accounting utilities the Commission has adjudged to represent asset value, and to be proper to be retained as a basis for rates and for charges to operating expense, as for depreciation.

The action of the Interstate Commerce Commission in failing to adopt said "original cost" provisions, which action is cited by the appellants, is of no significance as tending to support the assertion that they are unreasonable and arbitrary. The Interstate Commerce Commission has had little, if any, experience in the regulation of rates of public utilities, upon the basis of the value of the property of individual utilities, and involving utility claims for depreciation expense, and hence was not

in a position to appreciate the necessity for the regulations in question.

The action of twenty-two State commissions in urging the "original cost" provisions before the Interstate Commerce Commission, the action of the Federal Communications Commission in promulgating Order No. 7–C, the action of State commissions in adopting similar orders in various States, as in New York and Wisconsin, and in approving said accounting order through their National organization, and the action of the Federal Power Commission in adopting substantially identical provisions in its accounting order recently promulgated, are far more significant insofar as concerns the necessity, reasonableness, and alleged arbitrariness of such original cost provisions, than the failure of the Interstate Commerce Commission to adopt such regulations, after a brief argument before a single commissioner, without supporting evidence.

VII

The requirement of the Commission's Order, contained in Instruction 2 (b) 1 that "all charges to the accounts prescribed in the classification for telephone plant, income, operating revenues, and operating expenses shall be just and reasonable and any payments by the company in excess of such just and reasonable charges shall be included in Account 323, 'Miscellaneous Income Charges,'" is not arbitrary or unreasonable, nor

beyond the authority of the commission nor violative of the due process clause of the fifth amendment.

VIII

The instructions contained in said Order 7–C with respect to what property shall be entered in accounts 100.1, 100.3, and 103 do not deprive the appellants of their rights under the due process clause of the fifth amendment.

IX

The provisions of Order No. 7-C challenged by the appellants are severable from the other provisions of said order, and the validity of the order, as a whole, does not depend upon the validity of those provisions.

ARGUMENT

The original cost provisions of Order No. 7–C are not in violation of the due process clause of the fifth amendment of the Constitution

The appellants in their Statement of Points to be relied upon in this court (R. 601) assert that the original cost provisions of said order No. 7–C are in violation of the due process clause of the Fifth Amendment in that:

a. They require appellants to keep their property investment accounts so as to misrepresent their investment in property.

b. They prevent appellants from charging any depreciation expense on a part of their actual investment in depreciable property.

c. In effect, they require a retroactive change in the accounts of transactions entered into with governmental approval, the records of which have been correctly kept in accordance with rules prescribed by law.

d. They are unreasonably burdensome and expensive and serve no useful purpose except the recording of information which, when needed, could be made available, in supplementary statements, pursuant to Section 213 (c) of the Communications Act of 1934, at relatively minor expense and without causing the accounts to misrepresent the facts.

We will discuss these several points separately. But before doing that we desire to discuss generally the extent of the Commission's power to regulate accounts, the proper construction of the original cost provisions of Order No. 7–C, and the obvious purpose to be served by accounts kept in accordance with those provisions. This general discussion will be applicable to various of the points to be later separately discussed.

The Congress, in the Communications Act of 1934, has granted to the Federal Communications Commission power to regulate accounts in the broadest terms. The principal provisions of that statute relating to accounting are set forth in the margin.[1] Certain other provisions which supple-

[1] Sec. 220. (a) The Commission may, in its discretion, prescribe the forms of any and all accounts, records, and memoranda to be kept by carriers subject to this Act, in-

ment the provisions quoted in the margin will be hereinafter set forth in this brief in the course of our discussion of particular points.

In determining the extent of the power of Congress to regulate the accounts of telephone companies, and in construing the act under which such power has been delegated to the Commission, the legitimate purposes for which such power may properly be exercised will be taken into account.

The Communications Act does not state the purpose of the grant of power with respect to accounts aside from the general declaration found in Sec-

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cluding the accounts, records, and memoranda of the movement of traffic, as well as of the receipts and expenditures of moneys.

(b) The Commission shall, as soon as practicable, prescribe for such carriers the classes of property for which depreciation charges may be properly included under operating expenses, and the percentages of depreciation which shall be charged with respect to each of such classes of property, classifying the carriers as it may deem proper for this purpose. The Commission may, when it deems necessary, modify the classes and percentages so prescribed. Such carriers shall not, after the Commission has prescribed the classes of property for which depreciation charges may be included, charge to operating expenses any depreciation charges on classes of property other than those prescribed by the Commission, or, after the Commission has prescribed percentages of depreciation, charge with respect to any class of property a percentage of depreciation other than that prescribed therefor by the Commission. No such carrier shall in any case include in any form under its operating or other expenses any depreciation or other charge or expenditure included elsewhere as a depreciation charge or otherwise under its operating or other expenses.

(c) The Commission shall at all times have access to and the right of inspection and examination of all accounts, rec-

tion 1 of the Act which is set out below at page 23. However, the annual reports of public utilities, and the accounts on which they rest, serve various well recognized public purposes, some of which are recited on page 27 of the brief of the appellants. It is to be assumed that the Congress designed to promote these well recognized purposes among others, and especially that it designed to promote the purposes mentioned in said Section 1, including rate regulation.

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ords, and memoranda, including all documents, papers, and correspondence now or hereafter existing, and kept or required to be kept by such carriers, and the provisions of this section respecting the preservation and destruction of books, papers, and documents shall apply thereto. The burden of proof to justify every accounting entry questioned by the Commission shall be on the person making, authorizing, or requiring such entry and the Commission may suspend a charge or credit pending submission of proof by such person. Any provision of law prohibiting the disclosure of the contents of messages or communications shall not be deemed to prohibit the disclosure of any matter in accordance with the provisions of this section.

* * * * *

(h) The Commission may classify carriers subject to this Act and prescribe different requirements under this section for different classes of carriers, and may, if it deems such action consistent with the public interest, except the carriers of any particular class or classes in any State from any of the requirements under this section in cases where such carriers are subject to State commission regulation with respect to matters to which this section relates.

(i) The Commission, before prescribing any requirements as to accounts, records, or memoranda, shall notify each State commission having jurisdiction with respect to any carrier involved, and shall give reasonable opportunity to each such commission to present its views, and shall receive and consider such views and recommendations.

The appellants misconceive the purpose and the effect of the original cost provisions of Order No. 7–C. On page 21 of their brief they say:

> That part of the Commission's order which requires property purchased from another utility to be carried in the companies' investment accounts at the amount it cost that former owner which first devoted it to public use, and which requires that the difference between that figure and the amount paid for it by the accounting company be placed in an adjustment account, to be disposed of, written off, or amortized as the Commission may direct * * * obviously has its foundation in a theory that the cost to the predecessor company fixes the basis for rate making. No other explanation of these rules suggests itself.
>
> * * * To carry this theory to a logical conclusion, the Commission should have made a rule that the amount in the "adjustment" account should be immediately charged to surplus. In this respect the Commission lacked the courage of its convictions. Instead, it has attempted to avoid the issue by merely providing that amounts in the adjustment account shall be disposed of as the Commission may direct, without stating any principle on which it proposes to act. Its ultimate purpose may be carried out under cover of this power.

If the Commission entertains such "ultimate purpose" as the appellants suppose, and if in pursuance thereof it shall make an unlawful order,

any company affected may thereupon have recourse to the courts. Until such order shall have been made, however, the appellants will have no cause for complaint. *Norfolk & Western Railway Company* v. *United States,* 287 U. S. 134, 141. The appellants, however, for some reason undertake to support their claim that the original cost provisions of Order No. 7–C are unreasonable and arbitrary, and upon that ground unconstitutional by asserting this assumed "fallacious theory" of the Commission at the outset of their argument, on page 21, and as the first point set out in their "Summary" on page 18.

There is nothing in Order No. 7–C itself, nor to be found in the record, which justifies the assertion that the order rests upon a theory that the original cost of property when first dedicated to public use, whether such cost was paid by the present owner or by a predecessor company, "fixes the basis for rate making." The assertion of appellants that this is the theory upon which the order rests and the suggestion that the Commission entertains the "ultimate purpose" of exercising its rate regulatory powers upon that theory, attributes to the Commission an ignorance of the law, or a disposition to disregard the law, which this court will not attribute to that honorable body. It will be assumed that the Commission knows the fundamental rule of rate making laid down in *Smyth* v. *Ames,* 169 U. S. 466, and that it will be governed thereby.

While no proper use of original cost suggests itself to the appellants, such proper use will be obvious to the court. Original cost is not value, and does not fix value. It is, however, evidence of value.

The duties of a Commission, such as the Federal Communications Commission, extend far beyond the decision of cases instituted by complaints of those who receive utility service. The Commission has the affirmative duty to determine whether rate increases, when proposed by a utility, shall be permitted to take effect without suspension and investigation. It has likewise the continuing duty to consider whether the rates of each company subject to its jurisdiction which are in effect, and as to which no complaints have been made to the Commission, are such rates as to require no specific investigation by the Commission, or whether in any particular case they should be made the subject of a formal investigation, in a proceeding in which all interested parties may be heard, and in which whatever order is appropriate changing such rates may be made.

The provisions of the Communications Act of 1934 which impose the duties just mentioned upon the Federal Communications Commission are those immediately hereinafter set forth. The italics appearing therein are supplied.

> *Section 1. For the purpose of regulating interstate and foreign commerce in communication by wire and radio so as to make*

available, so far as possible, to all the people of the United States a rapid, efficient, Nation-wide, and world-wide wire and radio communication service with adequate facilities at reasonable charges, for the purpose of the national defense, and for the purpose of securing a more effective execution of this policy by centralizing authority heretofore granted by law to several agencies and by granting additional authority with respect to interstate and foreign commerce in wire and radio communication, *there is hereby created a commission to be known as the "Federal Communications Commission", which* shall be constituted as hereinafter provided, and which *shall execute and enforce the provisions of this Act.*

Section 201. (a) It shall be the duty of every common carrier engaged in interstate or foreign communication by wire or radio to furnish such communication service upon reasonable request therefor; and, in accordance with the orders of the Commission, in cases where the Commission, after opportunity for hearing, finds such action necessary or desirable in the public interest, to establish physical connections with other carriers, to establish through routes and charges applicable thereto, and the divisions of such charges, and to establish and provide facilities and regulation for operating such through routes.

(b) *All charges, practices, classifications, and regulations for and in connection with such communication service, shall be just*

and reasonable, and any such charge, practice, classification, or regulation that is unjust or unreasonable is hereby declared to be unlawful: * * *

SECTION 203 (a). Every common carrier, except connecting carriers, shall, within such reasonable time as the Commission shall designate, file with the Commission and print and keep open for public inspection schedules showing all charges for itself and its connecting carriers for interstate and foreign wire or radio communication between the different points on its own system, and between points on its own system and points on the system of its connecting carriers or points on the system of any other carrier subject to this Act when a through route has been established, whether such charges are joint or separate, and showing the classifications, practices, and regulations affecting such charges. Such schedules shall contain such other information, and be printed in such form, and be posted and kept open for public inspection in such places, as the Commission may by regulation require, and each such schedule shall give notice of its effective date; and such common carrier shall furnish such schedules to each of its connecting carriers, and such connecting carriers shall keep such schedules open for inspection in such public places as the Commission may require.

(b) *No change shall be made in the charges, classifications, regulations, or practices which have been so filed and published*

available, so far as possible, to all the people of the United States a rapid, efficient, Nation-wide, and world-wide wire and radio communication service with adequate facilities at reasonable charges, for the purpose of the national defense, and for the purpose of securing a more effective execution of this policy by centralizing authority heretofore granted by law to several agencies and by granting additional authority with respect to interstate and foreign commerce in wire and radio communication, *there is hereby created a commission to be known as the "Federal Communications Commission", which* shall be constituted as hereinafter provided, and which *shall execute and enforce the provisions of this Act.*

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(b) *No change shall be made in the charges, classifications, regulations, or practices which have been so filed and published*

except after thirty days' notice to the Commission and to the public, which shall be published in such form and contain such information as the Commission may by regulations prescribe; * * *.

SECTION 204. *Whenever there is filed with the Commission any new charge, classification regulation, or practice, the Commission may* either upon complaint or *upon its own initiative without complaint, upon reasonable notice, enter upon a hearing concerning the lawfulness thereof; and pending such hearing* and the decision thereon the Commission, upon delivering to the carrier or carriers affected thereby a statement in writing of its reasons for such suspension, *may suspend the operation of such charge, classification, regulation, or practice*, but not for a longer period than three months beyond the time when it would otherwise go into effect; *and after full hearing the Commission may make such order with reference thereto as would be proper in a proceeding initiated after it had become effective.* If the proceeding has not been concluded and an order made within the period of the suspension, the proposed change of charge, classification, regulation, or practice shall go into effect at the end of such period; but in case of a proposed increased charge, the Commission may by order require the interested carrier or carriers to keep accurate account of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts are paid,

> and upon completion of the hearing and decision may by further order require the interested carrier or carriers to refund, with interest, to the persons in whose behalf such amounts were paid, such portion of such increased charges as by its decision shall be found not justified. At any hearing involving a charge increased, or sought to be increased, after the organization of the Commission, the burden of proof to show that the increased charge, or proposed increased charge, is just and reasonable shall be upon the carrier, *and the Commission shall give to the hearing and decision of such questions preference over all other questions pending before it and decide the same as speedily as possible.* [Italics ours.]

Every commission vested with general regulatory powers such as those which have been imposed upon the Federal Communications Commission must exercise those powers as to every company subject to its jurisdiction. It is clear that its duties can not be properly performed unless the law provides means and instrumentalities whereby information may be available to the Commission as to the facts which are necessary to be known in order that the Commission may at any time form an intelligent judgment concerning the probable reasonableness and lawfulness of the rates of any of the numerous utilities subject to its jurisdiction.

The reports which companies are required to make, and the accounts upon which they rest, have

been designed to supply information for the consideration and guidance of the Commission. They serve the occasional purpose of supplying evidence for use in formal rate proceedings, and they serve the much more important purpose of supplying to the Commission information which it may use in the performance of its continuing duty to act or to withhold action on its own motion concerning the rates of each accounting utility.

To serve this latter purpose, the accounts must do more than carry information which can be searched for, and compiled, and reported upon, by expert accountants. They must classify and segregate and set forth the facts from which, as to any company, conclusions may be drawn as to the fair value of its property devoted to the public use, the expense of operating such property, and the income derived from such operation; and these facts must be shown in such manner that they may be quickly seen and considered. The Commission can not have frequently recurring audits made of the accounts of the great number of utilities over which it exercises jurisdiction. In order that it may do its work with proper expedition, the information which it desires must be available to it upon the face of the reports of each utility, so that it may be considered at any time without the great cost and the delays which are unavoidably involved in accounting investigations.

The requirements imposed upon public service corporations as to the form in which their accounts

shall be kept, and as to the reports they shall make, have been changed from time to time, and always for the purpose of increasing their usefulness to the public or to public officials; but such systems of accounts now in effect fall far short of meeting fully the needs of regulatory Commissions. Rate investigations are notoriously prolonged, and much of the delay is due to the fact that the accounts of utilities have not been so kept as to make the information they contain, or should contain, readily available. It results that prolonged accounting investigations are required to obtain and bring necessary evidence into formal proceedings from the accounts or other sources; and it results also that commissions are ordinarily compelled to reach their informal conclusions concerning the desirability of action on their own motion, by way of institution of formal proceedings, without information of facts which the reports of the utilities ought to make quickly and easily available.

The Uniform System of Accounts for Telephone Companies, prescribed by the Federal Communications Commission in its Order No. 7–C, and recommended by the National Association of Railroad and Utilities Commissioners to the State commissions for their adoption, represents an earnest attempt on the part of the regulatory commission of the country, both Federal and State, to improve the instrumentalities with which they work, so that they may perform their duties intelligently and with reasonable expedition.

In his dissenting opinion in *St. Joseph Stock Yards Co.* v. *United States,* 80 Supreme Ct. Advance Opinions, 679–672, Mr. Justice Brandeis commented on the long delays which have been incurred in the application of the rule of *Smyth* v. *Ames* in rate cases. These delays he referred to as seriously impairing the power of rate regulation, and as justifying the Congress in making the findings of fact of the Secretary of Agriculture in rate proceedings before him conclusive.

Commenting upon such delays, in the case then before the court, Mr. Justice Brandeis said:

> The history of this case illustrates that regulation cannot be effective unless the legality of rates prescribed may, if contested, be determined with reasonable promptness.

It is indeed essential to the effectiveness of regulation that it shall be possible with reasonable promptness to present to the courts the facts upon which the legality of prescribed rates may be determined, if such legality is challenged; but it is even more essential to the success of regulation that regulatory Commissions, themselves, for their current information and guidance, shall have knowledge of those facts upon which the legality of the rates they prescribe will be determined by the courts if they shall be challenged, so that they may prescribe rates which will meet the legal tests which have been laid down by the courts.

The rule in *Smyth* v. *Ames* 169 U. S. 466, is now conclusively settled, as a rule which must be followed when the constitutionality of rates is drawn in question. Furthermore it was held in *West* v. *Chesapeake & Potomac Telephone Co.,* 295 U. S. 662, that a Commission in its legislative proceedings must reach its conclusions from data which meet the tests established by judicial decisions.

The changes in accounting methods and practices which the uniform system of accounts here under attack requires are designed to make available to the Commission, upon the face of reports rendered by reporting utilities, the evidentiary facts necessary to be known by the Commission, which now are obtainable only at the cost of long and expensive accounting investigations.

The "original cost" provisions of the order do not require appellants to keep their property investment accounts so as to misrepresent their investment in property

The appellants assert in their Statement of Points that the original cost provisions of the order require them to keep their property investment accounts so as to misrepresent their investment in property (R. 601).

Upon this point the findings of the court are as follows:

III

Telephone Division Order No. 7–C requires plaintiffs to include in the telephone

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plant accounts the "original cost" of their telephone plant, and provides that the difference between said original cost and cost to the accounting company of property acquired from another public utility shall be recorded on their books in other specified investment accounts.

IV

Plaintiffs have heretofore performed accounting with respect to property acquired from other public utilities which resulted in the inclusion in their telephone plant accounts of amounts representing various costs, such as current cost new, actual cost to plaintiffs, structural value, or cost to the predecessor company (by merger of book accounts). The Uniform System of Accounts prescribed by Telephone Division Order No. 7–C requires that in accounting for property acquired from another public utility, and in all other instances, plaintiffs' telephone plant accounts shall be stated on a uniform basis, that being "original cost", as therein defined.

V

Telephone Division Order No. 7–C does not require that the recorded cost or investment of the plaintiffs in property theretofore acquired by them from another public utility be obliterated or eliminated from their investment accounts, but merely requires plaintiffs to segregate the element of recorded cost or investment into the following investment accounts:

100.1 Telephone plant in service.
100.2 Telephone plant under construction.
100.3 Property held for future telephone use.
100.4 Telephone plant acquisition adjustment.

VI

Telephone Division Order No. 7–C further requires plaintiffs to include in their investment accounts the amount which they actually pay for property acquired on and after January 1, 1936, from other public utilities.

IX

Telephone Division Order No. 7–C requires that plaintiffs' accounts shall be kept on a basis which will reflect the facts with respect to their transactions and which will show their actual condition for the information of all persons interested therein, except with respect to contributions to predecessor utilities and depreciation of property held for future telephone use, and said order is capable of practical application except with respect to contributions to predecessor utilities.

The appellants have excepted to Findings III, IV, and VI upon the assertion that Account 100.4 is not an investment account, and they also have excepted to Finding IX. The findings, however, are fully supported by the plain terms of the order itself, and likewise by the evidence. Reference is made to the affidavits of Norfleet, R. 469–477;

Bickley, R. 504–526 and R. 516–518; Colbert, paragraphs (A), (B), and (C), R. 525–526; Orton, paragraphs (A), (B), and (C), R. 534–535; Smith, paragraphs (A), (B), and (C), R. 545–546 and (A), (B), and (C), R. 547–548.

The appellants, to support their contention, rely upon arguments contained in affidavits of their accountants all of which assert the opinion that Account 100.4 is not to be regarded as an asset account. Appellants' affidavits are fully met by the affidavits offered by the Commission and just referred to. The discussion of the court below touching this matter is as follows:

> The new system requires that when telephone plant in service is acquired, the amount paid therefor shall be charged to account 276 (Telephone plant acquired). The original cost of the property, estimated if not known, shall then be charged (debited) to the appropriate telephone plant account, whether "in service" (100.1), "under construction" (100.2), or "held for future use" (100.3) and credited to account 276. After debits to 276 for "contributions", and for reserve requirements for depreciation and amortization to date of the plant acquired, the amount remaining in 276 shall be debited or credited as appropriated to account 100.4 (Telephone plant acquisition adjustment). As to 100.4, the system provides: "The amounts recorded in this account with respect to each property acquisition shall be disposed of, written off, or provision shall be

made for the amortization thereof in such manner as this Commission may direct (100.4 (c)). "Original cost" as used is defined as "the actual money cost of or the current money value of any consideration other than money exchanged for property at the time when it was first dedicated to the public use, whether by the accounting company or by a predecessor public utility" (instruction 3–S–1).

The plaintiffs direct at this requirement the objection that these provisions violate the fundamental principles of accounting in the following respects; although 100.1, 100.2, 100.3, and 100.4 if added together immediately will show the company's actual investment in its plant, since 100.4 must be written off at the will of the Commission, it will be necessary to carry a surplus reserve against this possible write-off. Once the write-off has been made, they declare that no combination of balances will reflect the company's actual investment. And they object further, because there can be no depreciation charge to any amount in account 100.4.

In considering the merits of these objections, it becomes necessary to examine, for purposes of comparison, the system now in effect which the plaintiffs do not attack as unreasonable and which they seek to retain. Under the present system, account 278 "undistributed cost of property" performs a function similar to account 100.4. Under it, when a purchase is made, the estimated cur-

rent value of the land, the current cost new (estimated if not known) of certain other telephone plant, the original cost of franchises, and the cost of uncompleted projects are charged to their corresponding accounts. After crediting to reserve accounts, the estimated depreciation and amortization applicable, the difference between the total of the foregoing amounts and the cost to the accounting company of the plant acquired is debited or credited to 278, "undistributed cost of property." Account 278 is classed as a "telephone plant account" and is reported in the balance sheet as part of account 100 (Telephone plant).

As an alternative, the Commission may permit the transfer of the amounts in the "telephone plant accounts" and in "depreciation and amortization reserve accounts" as carried in the books of the vendor company to the books of the purchaser. In some instances, the amounts actually paid by the purchasing companies have been recorded in the "plant" accounts. Thus, actual cost, current cost new at the time of purchase, and original cost at the time of first dedication are in use at present as the basis of various telephone plant accounts. The amount in 278 of the present system is subject to no depreciation and may be written off only through surplus

On a comparison of the two systems, that of this Commission seems to more accurately reflect the condition and record the history

> of the plant. Account 100.4 is listed among investments. It can be subdivided so that there can be segregated any amount therein not representing (1) the cost of elimination of competition; (2) payment to an affiliate at a price in excess of cost to it with a profit returnable to the purchasing company in the form of dividends or otherwise; and (3) any other element not expended in public interest.
>
> This segregated amount would receive the same treatment substantially in the rate and depreciation basis as would amounts appearing in 100.1 "Telephone plant in service." In this light, it appears that the proposed system merely provides segregation, and that the addition of the amounts in these investment accounts 100.1 through 100.4 would accurately picture the legitimate investments of the purchasing company (R. 566–568).

The appellants argue that after items have been written out of Account 100.4, no combination of figures appearing in Accounts 100.1 to 100.4, inclusive, will show the true investment of the company in its plant. They strenuously asert that this violates the fundamentals of correct accounting.

The contention involves the assumption that it is the right of the appellants to have their asset accounts show the total amount paid for property acquired regardless of the extent and condition of that property. The accounting system now in force, as prescribed by the Interstate Commerce

Commission, does not permit that, and this court has negatived that claim.

Under the accounting system now in force, while the cost of purchased property of an accounting company is entered in the asset accounts of the company, the estimated amount of reserve requirements applicable thereto is required to be credited to Account 171, "Depreciation Reserve" ((C) R. 366), to be carried as a liability. The principle is thus recognized that the accounts should state the asset value of the property purchased. The defect of the system lies in the fact that no method is provided for assuring that the full purchase price entered in the accounts represents consideration paid for asset value of plant property.

Under Order No. 7–C, the accounts of any company will show the total amount paid for any property unless and until the Commission shall require any amount recorded in Account 100.4 to be written off in whole or in part. If the extent and character of property purchased, and the facts affecting a particular case, are such as to satisfy the Commission that asset value was not obtained to the full amount of the purchase price paid in excess of original cost, so that the Commission is justified in requiring a company to write off any item or items of Account 100.4, in whole or in part, the asset accounts of the company will thereafter reflect not the total amount expended by the company in the acquisition of its property, but the

portion thereof which is represented by the asset value of property acquired and still in service. This is the proper purpose of asset accounts.

This was the question in principle which was involved in *Kansas City Southern Railway Company* v. *United States,* 231 U. S. 423. In that case the carrier improved its road by constructing certain new sections, and abandoning old sections where the grades were unduly heavy. The Commission required the cost of the abandoned sections to be written out of the carrier's accounts.

The Kansas City Southern contested the Commission's order upon the ground that the regulation was so entirely at odds with the fundamental principle of correct accounting as to manifest an abuse of power. In sustaining the Commission's order, the court said:

> The contention of the appellant that property, originally acquired because necessary in the construction of the road, and afterwards abandoned only because rendered unnecessary by the improvement and development of the property, should remain in the property account as a part of the stockholders' investment, will be found, upon analysis, to rest upon the unwarrantable assumption that all capital expenditures result in permanent accretion to the property of the company. This in effect ignores depreciation—an inevitable fact which no system of accounts can properly ignore. A more complete depreciation than

> that which is represented by a part of the original plant that through destruction or obsolescence has actually perished as useful property, it would be difficult to imagine (231 U. S. 306).

The right of an appellant to carry amounts in its asset accounts representing any given aggregate depends upon whether it has assets which represent those amounts. If it has, then there is nothing in Order No. 7–C which prevents carrying those accounts in its asset accounts. That order, as we have seen, requires only that where amounts in excess of the original cost of property have been paid by an accounting utility, the excess payments shall be recorded in Account 100.4, and subjected to the scrutiny of the Commission. If the facts are such as to justify the retention of any excess in whole or in part in Account 100.4, it there remains, to the extent justified, as a statement of asset value, but if the facts are such as to justify the Commission in requiring that the same be written off, then it will properly disappear from the statement of the company's assets, just as did the cost of the abandoned road bed in the *Kansas City Southern case.*

The aforementioned erroneous assumption of the appellants' accountants upon which rests appellants' contention that the original cost provisions of Order No. 7–C are arbitrary and unconstitutional, is itself based upon an insistent misunderstanding of the provisions of Account 100.4.

The appellants' Affiant Kester in his affidavit asserted as follows:

> The difference between the owner's investment and the investment of the prior owner *will be shown temporarily* in an "adjustment" account, *but this must be extinguished,* either immediately or later, at the pleasure of the Commission. * * * *It is true that so long as the "difference" remains in the "adjustment" account, it is technically listed as an asset of the company, but since its extinction is mandatory and may be immediate if the Commission so wills, it would not be regarded as an asset in anything but name.* The accounts list it as an asset, but label it as an asset to be charged off, and therefore impliedly worthless. In actuality, it is a deferred charge against surplus, since the Commission can make it such a charge at any time, and the company could not safely regard it except as a deduction from surplus. In practical effect, the situation is no different while the amounts in Account 100.4 are listed among the assets than it is after they are charged off (R. 327–328). [Italics ours.]

It is upon this construction, by which the Commission's order is made to require every item in Account 100.4 to be written off, that the appellant's contention rests. It is an erroneous construction.

That the amounts written into Account 100.4 are listed as assets while they there remain even the appellant's affiants admit. The Affiant Kester's language, touching this point, we have just quoted above. Mr. Sangster said:

> Said rules require that the actual cost of property purchased by the carrier from another utility shall be charged in part to one or other of the three accounts above mentioned and in part to account "100.4 Telephone plant acquisition adjustment." But, as previously noted, *the amounts standing in account 100.4 are subject to the arbitrary rule that they shall be disposed of* as directed by the Commission in some manner unknown to the accounting company. * * * In particular the balance sheet would show (as it must) an account designated "100.4 Telephone plant acquisition adjustment" which, to the minds of most persons reading the same, would be either unintelligible or would convey the impression that it represented *an asset of dubious character"* (R. 311–312). [Italics ours.]

Affiant Maddèn said:

> While the balance in account 100.4, Telephone Plant Acquisition Adjustment, is listed as an investment asset (p. 25), *the extinguishment of the balance is mandatory* (Account 100.4 C, page 28), and may be proximate or remote as the Commission may direct (R. 320). [Italics ours].

The Affiant Heiss said:

> The difference between the owner's investment and the investment of the prior owner will be shown temporarily in an "adjustment" account, but this must be extinguished, either immediately or later, at the pleasure of the Commission. *While this "difference" is technically listed as an asset of the company so long as it remains in the "adjustment" account, it will not be regarded as an asset in anything but name, since its extinction is mandatory* and may be immediate if the Commission so wills. The accounts list it as an asset, but label it as an asset to be charged off and therefore impliedly worthless. *In actuality it is a deferred charge against surplus, since the Commission can make it such a charge at any time* (R. 338). [Italics ours.]

It will be noted that the affiants are a unit in recognizing the character of Account 100.4 as an asset account, and that they treat the setting aside of the asset elements there listed as a characterization of them as "dubious" and "impliedly worthless" only because they understand that by the Commission's order they are required to be written off from surplus, so that the placing of an item in Account 100.4 has in effect stamped it as a "deferred charge against surplus."

The construction thus placed upon the language quoted from Account 100.4 disregards the obvious meaning of that language. "Disposed of, written

off, or provision shall be made for the amortization thereof" is made to mean always and only "written off."

This construction in effect rejects the words "disposed of", or treats them as purely tautological. A proper construction gives effect to all of the quoted words. They permit that any amount which is written into account 100.4 shall be treated in one of three ways. It may be (1) assigned to its proper place in the company's accounts and there retained; or (2) it may be written off forthwith, or (3) it may be marked for gradual extinction by amortization either through charges to operating expenses or to income.

The appellants' construction disregards the primary meaning of the phrase "disposed of", which is that here suggested, "to find a place or use for", and attributes to it instead its secondary meaning which is "to get rid of."

Funk & Wagnalls Practical Standard Dictionary defines "dispose" as follows:

> *Dispose*—1. To set in order; arrange; settle. 2. To direct the mind of; incline. 3. To order or appoint; regulate. 4. To make over; bestow, or alienate, as property; now generally dispose of. II. i. To arrange or settle something. *to dispose of.*—1. To find a place or use for. 2. To part with; get rid of.

Websters New International Dictionary defines "dispose" as follows:

> *Dispose,* v. t.—1. To distribute and put in place; to arrange; to set in order; as to dispose the ships in the form of a crescent. 2. To assign to a certain place or condition; opposit. 3. To regulate; adjust; settle; determine. 4. To deal out; to assign a use to; to bestow for an object or purpose; to apply; to employ; to dispose of. 5. To give a tendency or inclination to; to make ready; prepare; adopt; especially to incline the mind to; to give a bent or propension to; to incline to make inclined * * *.
>
> *Dispose,* v. t.—1. To arrange or settle matters finally; to make disposition of; * * *. 2. To bargain to make terms * * *. *to dispose of—a.* to determine the fate of; to fix the condition, employment, etc., of; to direct or assign for a use. *b.* to get rid of; to put out of the way; to finish with * * *.

The accountants who wrote the provisions of account 100.4, as adopted by the Commission, used the phrase "disposed of" as the lexicographers use it.

Any given item in Account 100.4 the Commission, upon the facts of a particular case, may "dispose of" by finding and assigning to it a proper place in the accounts of the Commission (and such proper place may be Account 100.4 where it will stand marked as an investment properly made by

the accounting utility in the acquisition of property, in excess of the original cost of that property to a prior owner), or the Commission may require that it be written off at once, or it may require that it be amortized over a term of years either through charges to income, or through charges to operating expenses, as for depreciation.

That this is the proper construction of the language under consideration is shown by the affidavits of the Commission's accountants who prepared the classification, and by the construction placed upon it by other utility accountants of broad experience.

Mr. Norfleet, who for 16 years was with the Interstate Commerce Commission, as Examiner, Chief Accountant, and Auditor, now Chief Accountant for the Federal Communications Commission who was the principal advisor of the Commission in the preparation of the new accounting system (R. 468–469) says:

> Affiants for plaintiffs say that the amounts to be recorded in Account 100.4 must be extinguished either immediately or later at the pleasure of the Commission, and that such amounts are a deferred charge against surplus, since the Commission can make it such a charge at any time. *This is purely speculative and unsupported by the system of accounts,* the general rules of which govern the disposition of items not specifically provided for. *The affiants may just as well have made the proper assumption, namely, that*

the disposition of the amounts to be recorded in Account 100.4, "Telephone plant acquisition adjustment" would be disposed of, after the character of the item had been determined, in a manner consistent with the general rules underlying the uniform system of accounts for the distribution of expenditures, according to their character, to operating expenses, income, surplus, or remain an investment (R. 476.) [Italics supplied].

The Affiant Bickley, formerly Chief Accountant of the Wisconsin Public Service Commission, and now Chief Accountant of the Telephone Investigation being conducted by the Federal Communications Commission, in his affidavit said:

I do not understand this to mean that the Commission shall direct telephone companies to write off all of the adjustment account by deductions from surplus. It is my opinion that the Commission has given recognition to the various factors which may account for the amount in the adjustment account and has provided for the individual consideration thereof in the light of the facts as they are determined. (R. 511.)

* * * Furthermore, *the Commission, in its administration of account 100.4, might direct that all or a part of an amount included therein be classified as amounts applicable to buildings, pole lines, etc., according to the facts in the case.* There is nothing in the system which prohibits telephone

> companies from making this classification. It may not be assumed, however, that all amounts included in account 100.4 can or should be identified with various classes of plant. For example, if the account includes an amount for going value, the propriety of distributing this intangible to the tangible classes of plant is very doubtful. In fact, Kester, in his published writings, says that "good will" should be reported separately on the balance-sheet. (R. 517.) [Italics supplied.]

Mr. Colbert, Acting Director of Accounts for the Wisconsin Public Service Commission, referring to the provisions of 100.4 in his affidavit, said:

> (B) In my opinion these instructions considered together mean that when the accounting utility shall have determined the amounts includible in Account 100.4, Telephone Plant Acquisition Adjustment, it should submit full details concerning the same to the Commission and that thereupon the Commission will issue such order regarding the disposition of the amounts as is warranted by the facts in the case. *This means that the amount might be permanently retained in the investment accounts,* depreciated or amortized over the life of the property, or subject to such other disposition as might be appropriate for the items included in Account 100.4. (R. 527.) [Italics supplied.]

Mr. Orton, Director of Research of the Public Service Commission of New York, for 17 years a

utility accountant with a varied experience, in his affidavit said:

> E. The Bills of Complaint and affidavits submitted therewith object to the provision of paragraph C of account 100.4, Telephone Plant Acquisition Adjustment, providing that "the amounts recorded in this account with respect to each property acquisition shall be disposed of, written off, or provision shall be made for the amortization thereof in such manner as this Commission may direct." *This provision is interpreted as meaning that the commission may arbitrarily, without hearing or justification as a matter of correct accounting, at any time require the writing off of any portion or all of the balances contained in this account. I do not so interpret it. I do interpret it as meaning that the Commission will decide in the case of each acquisition, or perhaps in the case of the initial entry effecting all of the present property of the company in the case of the amounts then entered as a whole, what the accounting procedure shall be; and that this decision will be made after hearing, if hearing is desired by the company concerned,* and will be based upon the general policy regarding accounting and the treatment of depreciation laid down by the Federal Communications Commission and its predecessor the Interstate Commerce Commission after extensive hearings and upon sound accounting practice (R. 535–536). [Italics supplied].

Whether the appellants will be injured by orders made under the provisions of Account 100.4 depends upon what the Commission understands the provisions of the accounts to require, and what it will accordingly direct the appellants to do to conform thereto.

Chief Accountant Norfleet is the man who presided over the conferences with State commission representatives preceding the adoption of the accounting order. He, more largely than anyone else, acted for the Commission in formulating the order, and by virtue of his position he will have supervision of its enforcement (R. 469–470). What he says as to the meaning of the requirements in question should be taken as the construction which the Commission gives to those requirements, and will follow in its enforcement thereof.

The appellants have cited the decisions of the New York courts in *New York Edison Company* v. *Maltbie,* 244 App. Div. N. Y. 685 and 271 N. Y. 103–685. We think it well to comment briefly upon the difference between that case and this case, which renders the New York opinions inapplicable here.

The construction placed by the New York courts upon the order of the New York Commission, like the construction of a statute of a state by the highest court of the State, must be taken to settle the meaning of that order in New York, where the same was designed to have application. What the New York Commission's order required was stated in the opinion of the Appellate Division of the Su-

preme Court (sustained in a memorandum opinion by the Court of Appeals) as follows:

> * * * Account 143 is entitled "suspense to be amortized." This account, as required by the first paragraph of the instructions in relation thereto, is to "include losses in service value of property retired from causes for which provision has not been made in the depreciation reserves and losses from retirements which could not reasonably have been foreseen and provided for." It also "shall include any excess cost to the company of property purchased over the amount which is determined by the commission" to be the amount which the property cost the first public utility owner. The ultimate disposal of items placed in this account is shown by the last paragraph of the instructions. "Charges shall be made to this account only upon order of the Commission and *shall be written off* over such period and in such manner as the commission may by order prescribe." [Italics ours.]

It thus appears that any amount paid by a utility upon acquisition of utility property in excess of the original cost of that property was, by the New York order, *marked for amortization without inquiry, and without regard to facts which might justify such payment and render the amount paid a true statement of asset value. The order itself left no alternative disposition open. Without exception every item representing any such excess pay-*

ment was to be written out of the accounts of the utility by which the same was made.

Under the order of the Communications Commission, in contrast, as we have pointed out, each such payment is to be subjected to the Commission's scrutiny in the light of the facts surrounding the same, and if such facts warrant, it will "otherwise dispose of" the item than by causing the same to be either written off at once or amortized. The order of the Commission is flexible, permitting the requirement imposed in each particular case to be determined by the facts of that case.

This quality of flexibility was wholly absent from the New York case. Upon this point the court below said:

> This flexibility distinguishes the system at bar from that held invalid in *New York Edison Company* v. *Maltbie,* 244 A. D. (N. Y.) 685 (R. 568).

The "original cost" provisions of the order do not "prevent appellants from charging any depreciation expense on a part of their actual investment in depreciable property"

The appellants assert that the provisions of order No. 7–C "prevent appellants from charging any depreciation expense on a part of their actual investment in depreciable property." This assertion refers to the amounts recorded in Account 100.4.

It is not true that no depreciation may be charged against the amounts, in Account 100.4. It is true that no depreciation upon such amounts may be charged except as the Commission, after consideration of the facts in any case, may permit; and it is also true that such amounts as are permitted are charged to "Amortization of intangible property", Account 613, instead of being denominated "Depreciation" and charged to Account 608 (R. 186). As we have before pointed out, the effect of Order No. 7–C is simply to set aside amounts recorded in Account 100.4 for the consideration of the Commission, and for disposition according to its order. It is to be presumed that the Commission will be governed by the facts in each case; and that when, and to the extent that, such amounts represent payments which ought properly to be depreciated through amortization charges to operating expense, it will so order. If, upon application, in a proper case it shall fail to grant its permission for proper charges to operating expense, the company is not without remedy, as was pointed out in the opinion below, hereinafter quoted.

We recognize that this limitation upon the appellants in the matter of their charges for depreciation, whereunder they may not charge depreciation upon items recorded in Account 100.4 without justifying such charges to the Commission, is probably the gravest objection to Order No. 7–C from their point of view. At the same time it consti-

tutes one of the most necessary provisions of the order for the promotion of the essential purposes of the Communications Act.

The point at issue is very plain. At page 25 of their brief, the appellants state as follows:

> Furthermore, the Commission should not have any discretion in the matter. If depreciation charges are to be based on cost there should be an absolute rule for using a company's own cost as the basis, and not the cost of another company.

Under Order No. 7–C, the basis for depreciation charges, so denominated, is made the original cost of the property depreciated when it was first dedicated to the public use. The duty of the rate paying public to keep that investment good through operating expense is recognized, regardless of changes in ownership of the property; but the charging to operating expense of anything beyond the amount necessary for that purpose, under the guise of depreciation, is forbidden unless and until permitted by the Commission upon a showing of justification therefor upon the facts in the particular case where such charge is to be made.

It has been demonstrated to this court in former cases, in which some of the principal appellants were parties, that unjust exactions have been long practiced upon the public through overcharges for depreciation. *Lindheimer* v. *Illinois Bell Telephone Company,* 292 U. S. 150. *Northwestern Bell Telephone Co.* v. *Nebraska State R. Commission,*

Vol. 80, No. 10, Supreme Ct. Advance Opinions, 552.

This case is the first in which it has been asserted in this court that a public utility has a constitutional right to compute and record depreciation upon the entire amount which it may have paid for depreciable property regardless of the relationship between seller and purchaser, and of other circumstances surrounding the transaction, and of the actual value of the property purchased. The decision of this court in *United Railways* v. *West*, 280 U. S. 234, we submit, negatives this asserted right.

The appellants argue that the cited case was a rate case, and hence inapplicable. It can not be inapplicable unless it shall be held that, for some reason inherent in the Constitution of the United States, Congress has no power to require that public utilities shall restrict charges upon their books to operating expense for depreciation to amounts which approximate the depreciation actually incurred.

The true purpose of depreciation accounting and the possibility of its abuse were succinctly stated by this court in *Lindheimer* v. *Illinois Bell Telephone Company*, 292 U. S. 150, as follows:

> Broadly speaking, depreciation is the loss, not restored by current maintenance, which is due to all the factors causing the ultimate retirement of the property. * * * According to the practice of the Company, the depreciation reserve is not held as a sepa-

> rate fund but is invested in plant and equipment. As the allowances for depreciation, credited to the depreciation reserve account, are charged to operating expenses, the depreciation reserve invested in the property thus represents, at a given time the amount of the investment which has been made out of the proceeds of telephone rates for the ostensible purpose of replacing capital consumed. If the predictions of service life were entirely accurate and retirements were made when and as these predictions were precisely fulfilled, the depreciation reserve would represent the consumption of capital on a cost basis, according to the method which spreads that loss over the respective service periods. But if the amounts charged to operating expenses and credited to the account for depreciation reserve are excessive, to that extent subscribers for the telephone service are required to provide in effect capital contributions, not to make good losses incurred by the utility in the service rendered and thus to keep its investment unimpaired, but to secure additional plant and equipment upon which the utility expects a return (292 U. S. 167, 168, 169).

That, as a matter of current bookkeeping, it is not practicable to make entries upon the basis of a shifting value is quite true. The discussion quoted in appellants' brief from *Telephone and Railroad Depreciation Charges,* 177 I. C. C. 351, had relation to this difficulty. The reasons which led the Interstate Commerce Commission in that case

to refrain from attempting to base depreciation charges upon the value of property were stated in the paragraph immediately following that which is quoted in appellants brief, as follows:

> Beyond question, the evidence before us strongly supports the use for accounting purposes of original cost to the accounting company as the basis for depreciation charges. It is a method which can be readily applied, ensures a high degree of stability in operating expenses, and enables managements to anticipate future needs with reasonable confidence. On the other hand, the present value method would be difficult to apply and supervise, and would tend toward instability and uncertainty. Added to this, we have a record in which the representatives of State commissions and municipalities, the telephone companies, and the gas and electric companies are all agreed that originial cost should be used as the base; we have accounting regulations for all classes of carriers which have been in effect for many years, which uniformly prescribe original cost (or ledger value) as the base, and which have never been contested in court, or until recently even criticized, because of this fact; and finally we have evidence that the use of original cost as the base for depreciation charges has been approved by numerous other Federal and State authorities, including the Supreme Court of the United States for income tax purposes, and that this is the base which is in general

> use in the business world. The evidence is ample to show that the use of this base is "sustained by expert opinion and approved by experience" and that it "is not arbitrary in the sense of being without reasonable basis" (177 I. C. C. 381).

Considerable light upon the problem which confronts regulatory commissions may be obtained from a reading of the very able report which has thus been brought to the attention of the court by the appellants. If the brief paragraph quoted by them would give the impression that it was the opinion of the Interstate Commerce Commission that no attempt should be made to make recorded depreciation charges coincide as closely as possible with expired service value, a glance at that part of the report beginning at page 397 under the caption "Depreciation in Accounting and in Valuation" will remove that impression. We quote the following:

> In our prior report we pointed out the direct and intimate connection between the accrued depreciation of a property which must be considered in its valuation and the annual charges for accruing depreciation which should be included in the accounts. This connection has been recognized from the beginning by the railroads and furnishes the key to their contentions. * * * The telephone companies, however, repudiate the logic of their own position with respect to depreciation expense and deny, appar-

ently, that it has any intimate relation to depreciation in valuation. * * * They also say that our declaration on page 356 of the prior report that "it is essential to bear in mind, however, that there is an inseparable connection between the straightline method and the principle that accrued depreciation represented by the reserve must be deducted in ascertaining the rate base value", and similar statements appearing elsewhere in that report, are contrary to fact and law. It appears, moreover, from evidence of record, that in rate cases before State commissions the telephone companies contend that their depreciation reserves should be disregarded in valuation, and that for the latter purpose depreciation should be limited to the observed deterioration of the property. It was shown, for example, that one telephone company having a depreciation reserve equal to about 30 per cent of the recorded investment in the property contends that the depreciation for valuation purposes is no more than 9 per cent; and this illustration is typical. * * * The present position of the telephone companies, as we understand it, is that the accounting does not purport to follow the actual rate of consumption of property during individual accounting periods; that it is equitable, and sound as a matter of practical accounting, to spread the depreciation expense in equal annual charges over the service life of the property in question; but that the actual

> rate of consumption, and hence of accrual of depreciation, may be quite different (177 I. C. C. 397, 398, 399).

The Interstate Commerce Commission did not approve the position taken by the telephone companies, but stated its conclusion as follows:

> We have no difficulty in reaching the conclusion that the real measure of depreciation is the extent to which service capacity has been exhausted; that wear and tear, obsolescence, inadequacy, etc., are all factors in depreciation, information as to which constitutes evidence to be given appropriate weight in determining the extent to which service capacity has been exhausted; that although inspection may be helpful, the best estimate of the exhaustion of service capacity as of a particular date can be made only by a careful analysis of past experience and the application of informed judgment as to future trends; that, with the possible exception of the effect of insufficient maintenance, such an analysis will provide a more reliable estimate of the loss in service capacity than observation alone; *and finally that the principles are identical which govern the estimating of loss in service capacity for both accounting and valuation purposes* (177 I. C. C. 408). [Italics ours.]

Touching this matter of depreciation, the court below said:

> This complaint (that the order prevents charging depreciation upon amounts recorded in account 100.4) anticipates arbi-

> trary action by the Commission, under 100.4 (c) which authorizes handling of this item through amortization. The effect would be the same as writing down through depreciation, and until the Commission acts so that the accounts become so contrary to the principles of correct accounting as to constitute the Commission's order arbitrary and unreasonable, the Commission is within its powers. The court need not agree the accounting proposed is the best method, but at this stage it cannot be said the provision is arbitrary. The objection is made that the Commission's refusal to act properly within 100.4 (c) would constitute a negative order, nonreviewable within the doctrine of *Proctor & Gamble* v. *United States,* 225 U. S. 282. This would not cut off the plaintiff's right of attacking the system as it would apply to them after such refusal. The appeal need not be on the order denying relief but can be against the system as its operation is affected by such denial (R. 568).

The evidence relating to this matter of depreciation upon items recorded in Account 100.4 may be found in the affidavits presented by the Commission as follows: Norfleet, paragraph 23, R. 276; Bickley, R. 512; Orton, paragraph G, R. 537; and Smith, R. 550. The statement of Chief Accountant Norfleet is as follows:

> 23. The Commission's system of accounts looks specifically to allowing telephone companies to recover, through charges to operating expenses for depreciation, the

> "original cost" of depreciable property. It also looks to segregating such "original cost" from the cost of acquiring property from predecessor companies and further to the recovery of the differences, if the conditions and circumstances contributing to such differences warrant recovery, through charges to operating expenses for amortization (R. 476).

Where various constructions of an order of a Commission, or of a statute, are possible, the court will not choose that which would make its constitutionality doubtful, but the reverse, for the reason that the court will not presume upon the part of the legislature, or its agent, the purpose to exceed its powers. On this point we call attention to the construction by this court of the South Carolina Motor Vehicle Act, in *Hicklin et al.* v. *Coney et al.*, 290 U. S. 169, 176. In that case the construction placed upon the act by the South Carolina Commission, as shown by the affidavit of the Superintendent of its Motor Transportation Division, was accepted as showing the effect of the statute upon the complaining truck owner. We quote from the opinion:

> The State court did not express disagreement with the Commission's construction * * *. Nor have we anything before us to show that the statute is being enforced and the exemption construed in any other sense. Upon the present record, it appears that the exemption is applied with two limi-

tations, first, that, as construed by the state court, it can refer only "to one whose principal business is that of a farmer or dairyman and not to one merely incidentally engaged in farming or dairying", and, second, under the construction of the Commission in enforcing the statute—a construction not disapproved by the state court—that it applies only to farmers and dairymen who occasionally, and not as a regular business, transport farm or dairy products for compensation. We cannot say that a classification based on such a use of the highways is an arbitrary one and thus encounters constitutional objection (290 U. S. 169, 178).

See also *Interstate Commerce Commission* v. *Oregon-Washington Railway and Navigation Co.*, 288 U. S. 14, 41, and *Kansas City Southern Railway Co.* v. *United States*, 282 U. S. 760, 764.

Upon this point the finding of the court below was as follows:

VIII

The plaintiffs are not prevented by Telephone Division Order No. 7–C from recovering amounts included in Account 100.4 in view of the alternative provisions of paragraph (C) of the text of said Account 100.4, which make provision for the amortization or other appropriate disposition of amounts included in Account 100.4. The Commission has made no direction with respect to the disposition of any such amounts (R. 575).

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The "original cost" provisions do not "require a retroactive change in the accounts of utilities subject thereto"

The order does not require a change in the record of accounts of utilities which have been kept in the past, as appellants in their Statement of Points assert (R. 601). It requires that henceforth certain accounts shall be kept in a different form than heretofore. This will necessitate a recasting of accounts, just as every other system of accounts has required a recasting of accounts as theretofore kept, insofar as changes were deemed necessary and prescribed. This is very forcibly pointed out by Mr. Orton, Director of Research and Valuation of the Public Service Commission of New York, in his affidavit (Paragraph H., R. 537), and by Chief Accountant Norfleet of the Federal Communications Commission (Paragraphs 32 and 33, R. 479).

The "original cost" provisions are not "unreasonably burdensome and expensive", and they will serve important purposes that can not be equally well otherwise served

Original cost, as we have before said, is a relevant factor in the determination of value repeatedly recognized by this court. Congress has recognized its importance, and has expressly authorized the Commission to require its ascertainment or estimation. Section 213 (c) of the Communications Act provides as follows:

> (c) The Commission may at any time require any such carrier to file with the Com-

mission a statement showing the original cost at the time of dedication to the public use of all or of any part of the property owned or used by said carrier. For the showing of such original cost said property shall be classified, and the original cost shall be defined, in such manner as the Commission may prescribe; and if any part of such cost cannot be determined from accounting or other records, the portion of the property for which such cost cannot be determined shall be reported to the Commission; and, if the Commission shall so direct, the original cost thereof shall be estimated in such manner as the Commission may prescribe. If the carrier owning the property at the time such original cost is reported shall have paid more or less than the original cost to acquire the same, the amount of such cost of acquisition, and any facts which the Commission may require in connection therewith, shall be reported with such original cost. The report made by a carrier under this paragraph shall show the source or sources from which the original cost reported was obtained, and such other information as to the manner in which the report was prepared, as the Commission shall require.

Upon this point the court below said:

> The requirement that original cost be set forth in accounting records of the telephone companies serves to complete the picture of value in revealing the property's financial

> background and showing the relationship of a carrier's monetary return to the original as well as to its own investment. It aids the Commission in its duty to determine from all the pertinent circumstances and factors the just and reasonable rates which the carrier may exact from its service. Original cost is a relevant factor. *Smyth* v. *Ames,* 169 U. S. 466, 547; *Los Angeles Co.* v. *R. R. Comm.,* 289 U. S. 287, 306, cf. paragraph 213 (a) of the Act. The object of the system of accounts might well be to display the pertinent financial operation and throw light upon its present condition. *Kansas City Southern Ry.* v. *U. S., supra,* at p. 440. Original cost as a segregated item on a balance sheet may serve to reveal actualities which may be pertinent in fixing a rate base on the capitalized earning power of a property purchased. In making readily available facts which would tend to expose discrepancies in valuation, it cannot be said the system is so arbitrary as to be beyond the commission's power (R. 566).

While conceding the relevancy of original cost in valuation proceedings, and the right of the Commission to call for the same under the provisions of Section 213 (c), the appellants object to the showing of such original cost upon the face of their accounts. Their argument is based upon the assertion that such information will be usable only in valuation proceedings, and that the statement of the same in the accounts is a useless expense.

Whether the segregation and showing of original cost is useful or not is a matter which has been committed by Congress to the Commission for decision. Power has been granted in the broadest terms. The act provides:

> Sec. 220 (a). The Commission may, in its discretion, prescribe the forms of any and all accounts, records, and memoranda to be kept by carriers subject to this Act, including the accounts, records and memoranda of the movement of traffic, as well as of the receipts and expenditures of moneys.

It is for the Commission to determine what accounts shall be set up, and in what manner the accounting companies shall subdivide and show therein their investments, the business which they do, and the revenue which they receive therefrom, and the expenses which they incur in connection therewith.

Discussing the exercise of power granted to the Interstate Commerce Commission in the identical language of the above quoted Section 220 (a) (which in the Interstate Commerce Act is Section 220 (5)) this court has said:

> Within broad limits that body's determination is necessarily beyond revision and correction by the courts. * * * If we were in disagreement with the Commission as to the wisdom and propriety of the order, we are without power to usurp its discretion and substitute our own (*Norfolk & Western Ry.* v. *United States,* 287 U. S. 134, 141).

The rule as established by decisions of this court was succinctly stated by Judge Soper, in handing down the decision of a statutory court in *Chesapeake & O. Ry. Co.* v. *United States et al.*, 5 Fed. Supp. 14, as follows:

> It is well settled that, if an attack upon the accounting methods prescribed by the commission is to be successful, it must rest at bottom upon a showing that they are so entirely at odds with fundamental principles of correct accounting as to manifest an abuse of power. So long as the commission acts fairly and reasonably within the granted power conferred by Congress, its orders are not subject to review. *Kansas City Southern Ry.* v. *U. S.*, 231 U. S. 423, 444, 456, 34 S. Ct. 125, 58 L. Ed. 296, 52 L. R. A. (N. S.) 1; *Norfolk & Western Ry.* v. *U. S.*, 287 U. S. 134, 141, 53 S. Ct. 52, 77 L. Ed. 218. (5 Fed. Supp. 14.)

In *Kansas City Southern Railway* v. *United States*, 231 U. S. 423, 452, this court had before it a case where the Interstate Commerce Commission had required the cost of considerable sections of abandoned road bed to be charged to operating expenses. The railroad protested that if such cost was to be written off at all, it should be charged to surplus. In its opinion, touching this point, the court said:

> The suggestion apparently has force; but, upon consideration, we are unable to see that it furnishes ground for judicial inter-

ference with the course pursued by the Commission. Except for the contention (already disposed of) that the value of the abandoned parcels should be permanently carried in the property account as part of the cost of progress, it is and must be conceded that sooner or later it must be charged against the operating revenue, either past or future, if the integrity of the property accounts is to be maintained; and it becomes a question of policy whether it should be charged *in solido* to profit and loss (an account presumptively representative of past accumulations) or to the operating accounts of the present and future. If abandoned property is not charged off in one way or the other it remains as a permanent inflation of the property accounts, and tends to produce, directly or indirectly, a declaration of dividends out of capital. If it be charged off to the surplus account, it tends to prevent the declaration of dividends based upon a supposed accumulation of past earnings. If charged to operating expenses of the current and future years, it has a tendency to prevent the declaration of dividends from current earnings until the amount of the depreciation shall have been made up out of the earnings.

But, did we agree with appellant that the abandonments ought to be charged to surplus or to profit and loss, rather than to operating expenses, we still should not deem this a sufficient ground to declare that the Commission had abused its power. So long

> as it acts fairly and reasonably within the grant of power constitutionally conferred by Congress, its orders are not open to judicial review (231 U. S. 423, 456).

That the purposes to be served by showing the investment of an accounting company, in the manner provided by the order of the Communications Commission, are of such character as to mark the Commission's action as "fairly and reasonably within the grant of power" contained in Section 220 (a) of the act, is, we believe, quite clear. One of the Commission's most important duties, as we have before indicated, is that of acting as the guardian of the public interest with respect to rates. When rate changes are proposed, which to the Commission seem likely to affect the public interest unjustly, it is the Commission's duty to suspend the same and to permit the changes to take effect only after the Commission has become satisfied as to their reasonableness; and likewise whenever rates in effect appear to the Commission to be unreasonable in any respect, it is the Commission's duty, upon its own motion, to enter upon an investigation in which the justice and reasonableness of such rates may be passed upon, and other rates prescribed if the facts warrant.

It is obvious that the information which accounts, kept as prescribed by the Commission's order, will supply will be of great value to the Commission in the performance of this duty. The original cost of all property will be shown. What this

information will be was stated by the Commission's Chief Accountant, Mr. Norfleet, in his affidavit as follows:

> 18. With respect to property acquired from another public utility, the accounting performed under this Commission's system will disclose, by a simple combination of appropriate accounts, the following information in the accounts of the purchasing company:
>
> (a) The cost of the property to the accounting company.
>
> (b) The original cost (as defined in instruction 3S–1 of the uniform system of accounts) of the telephone plant, governmental franchises, and other similar rights acquired.
>
> (c) The amounts of depreciation and amortization applicable to the property represented by item (b) above.
>
> (d) The original cost of telephone plant under construction at date of purchase.
>
> (e) The original cost of property held for future telephone use acquired in the purchase.
>
> (f) The amounts contributed to the predecessor company or companies for construction and acquisition of the telephone plant acquired.
>
> (g) The net of all the foregoing amounts segregated and shown separately in the balance sheet in an account styled 100.4, "Telephone plant acquisition adjustment" (R. 474–475).

If there is an approximate correspondence, in the case of any utility between the original cost of its property, as shown by its accounts, and the amount which the utility paid for the same property, the Commission will naturally consider that the amount paid (in the absence of any contrary claim by the utility or on behalf of the public) should be considered as probably approximating a proper rate base. If, however, there is a great and unexplained excess of alleged cost of acquisition over and above what the property originally cost, the Commission will properly make some investigation before accepting the price paid as a proper base either for the determination of a fair return or for the determination of annual depreciation charges.

To be useful for the purpose just mentioned, with respect to the great number of companies subject to the jurisdiction of the Commission, the original cost must be easily available upon the face of the annual reports rendered by utilities to the Commission. In a rate case a company may, if it will, claim that amounts additional to original cost, as recorded in the accounts, must be included in the investment in operating property to be considered in fixing the rate base, or it may claim that the income or expense accounts overstate or understate actual income or expense. It can not be denied, however, that accounts kept in accordance with the provisions of Order No. 7–C will enable relevant facts to be expeditiously shown, which now can be

shown only after prolonged accounting investigations.

The appellants have laid stress upon the alleged difficulty and cost which may be involved in a recasting of their accounts so as to show the original cost of properties acquired by them from predecessor utilities. That they have greatly exaggerated such difficulty and cost appears from the affidavits filed by the Commission. (See paragraph D, Affidavit of Mr. Bickley, R. 510.) On this point Chief Accountant Norfleet, of the Communications Commission, in his affidavit stated:

> The Commission's system recognizes the fact that plaintiffs may encounter difficulty in identifying in the accounts and records, the original cost of some of the property which was acquired by purchase from a predecessor public utility and is now in existence in telephone service. Provision has been made for such difficulties by stating in the text of Account 100.4, "Telephone plant acquisition adjustment", that if the actual original cost is not known, the entries in this account shall be based upon an estimate of such costs (R. 477).

The provision of the Commission's order referred to by the affiant is to be read in connection with the general instructions contained in the order, 21 (B) (1) (R. 108) and 25 (D) "Determination of original cost" (R. 114). This last instruction, while, as appearing in the classification, having reference to "Telephone plant retired", supplies

a method for convenient determination of original cost which has already been approved by the Commission, and is open to the use of any telephone company.

The Commission's order imposes no burdensome restrictions upon companies with respect to such estimates as they may find it necessary to make. Under the order, whenever reasonable effort does not disclose recorded original cost, the accounting company is free to estimate such cost in its own way, holding itself prepared, as provided in general instructions 21 (b) (1) (R. 108), to inform the Commission as to the methods used. With such latitude allowed, no undue expense will be imposed upon the accounting companies by the original cost requirements of the Commission's order.

Whatever expense may be incidental to conformity to the original cost provisions of the order will be principally incurred in the ascertainment or estimation of "original cost." This expense Congress has expressly authorized the Commission to require by Section 213 (c) of the act, which has been set out on page 64 of this brief.

The provisions of the Commission's order that the amount recorded in account 100.4 "shall be disposed of, written off, or provision shall be made for the amortization thereof in such manner as this Commission may direct" is not a requirement which exceeds the power of the Commission

The appellants assert that the requirement that amounts recorded in account 100.4 "shall be dis-

posed of, written off, or provision shall be made for the amortization thereof in such manner as this Commission may direct", is void as beyond the power of the Commission. This is the second point in their Statement of Points (R. 601). Their argument is that the Commission's power is limited to the making of rules, regulations, and classifications in accordance with which all telephone companies, or all within a class, shall keep their accounts, and that it has no authority to require a specific accounting entry, with respect to a particular item or transaction.

If this be true the Commission's power is sadly inadequate, for it is obvious that telephone companies in purchasing operating property from other utilities may pay in excess of original cost therefor for a variety of reasons. Some of these were stated by the affiant Bickley as follows:

> It is my knowledge, based upon experience in analyzing the transactions of public utilities, that an *excess of cost to* an accounting company over the original cost of property purchased is due to a variety of elements, such as, (a) payments made by purchasing companies for going value and water power value, (b) differences in price levels, (c) a capitalization of advantages expected to be derived through the merger of plants and the integration of systems, and (d) payment made by the purchasing company for an opportunity to enter what it considers to be profitable territory (R. 511).

Some of the elements thus taken into consideration are proper to be considered in fixing the base upon which to compute rates and annual depreciation charges, and some are not. No universal rule can be laid down which will fit the facts of each particular case. To require that all amounts in excess of original cost shall be written off from surplus would be unjust to some accounting utilities. To permit all to be amortized by charges to operating expenses, in the nature of depreciation charges, or to permit all to remain permanently in the asset accounts for consideration in fixing the rate base would be unjust to the public.

Full justice can be done to utilities and to the public alike only by provisions such as here involved, which permit the Commission by administrative orders to bring the accounts of utilities into conformity with the facts of particular cases as they may be shown.

In addition to the broad grant of power in Section 320 (a), already quoted, Section 4 of the act, creating the Commission, contains the following paragraph:

> (i) The Commission may perform any and all acts, make such rules and regulations, and issue such orders, not inconsistent with this Act, as may be necessary in the execution of its functions.

We have already pointed out the necessity, in order that the Commission may execute its functions, that the accounts of each utility shall make

easily available information upon which conclusions may be formed as to the approximate rate base, and as to the approximate operating revenues and operating expenses.

What the appellants are contending for, as an alleged constitutional right, is the privilege of overstating their properties in their plant accounts (whenever in their inter-company transactions they have passed the title of operating properties between themselves at excessive prices) and of holding out to the Commission and to the public such overstated accounts as their true investment in property devoted to the public service, and the privilege also of charging to operating expense depreciation computed upon such overstated accounts.

The court will know, as all men know, that in the years prior to the recent depression, the public utility field was invaded by exploiters who in many instances consolidated public utility properties not primarily to enlarge their operations and reduce operating costs, but to make profit through sale of an increased volume of securities.

The device of the holding company has facilitated this exploitation. Often transfers of property have been made between companies controlled by the same holding company, and prices bearing no real relation to values were paid in securities of the so-called purchasing company. Prices so paid are of no aid to a regulatory commission in determining the probable reasonableness of rates, and

they constitute no proper basis for charges against the public for depreciation.

It is obvious that if the accounts of public utilities are to be made effective instrumentalities for supplying to regulatory commissions the information which they require, to enable such commissions to exercise their regulatory functions effectively, commissions must have the power to examine into these statements of cost of property, and to require any company to make such changes in its accounts as to cause them to state the facts as to property, and as to actual revenues and disbursements, which they purport to state, and in a manner uniform with other companies.

Under Order No. 7–C, the accounts of all utilities will show the original cost of all operating property on a uniform basis—that is, upon the basis of such cost at the time the property was devoted to the public use, and they will show also, in Account 100.4, the additional cost, in excess of original cost, which accounting companies have incurred in acquiring title from predecessor companies. The accounts will show also the extent to which the Commission has adjudged such excess costs proper to be retained as a basis for rates, and for amortization by annual charges to operating expense, and the extent to which it has adjudged the same not representative of asset value, and hence to be written off from surplus or amortized out of income. Such an order is clearly within the grant of power to the Commission.

In *Accounting Rules for Telephone Companies*, 203 I. C. C. 13, in which the Interstate Commerce Commission dealt with proposals of State commissions for a revision of the uniform system of accounts for telephone companies promulgated November 12, 1932, the following statement is made:

> It appears from the record that the *chief concern of the State commissions* as to whether the accounting for telephone plant purchased should be on the basis of original cost or current cost new *is related to the distribution of the proper amounts to the primary plant accounts for depreciation and amortization purposes* (R. 45). [Italics ours.]

It is evident from this so-called report of the Interstate Commerce Commission that there was no hearing before that Commission at which witnesses were heard in support of the State proposals. On this point the following is stated:

> It appearing that the presentation on behalf of the State commissions would be in the nature of argument, the presiding commissioner announced at the opening of the hearing that none of those who participated would be sworn, but that they would be subject to interrogation by all interested parties (R. 17).

Undoubtedly at that hearing the necessity of a change in accounting requirements to enable regulatory commissions to restrict annual depreciation

tion charges to amounts properly related to the extent of the properties depreciated was stressed; but it should be made clear that the State commissions desire original cost to be shown upon the face of utility accounts so that the same may be available for all uses—for rate regulation as well as for regulation of depreciation charges.

In the appellant's brief a statement is contained at page 19 as follows:

> The system prescribed by the Communications Commission has been rejected by the Interstate Commerce Commission, and held invalid by the courts of New York under a similar State statute.

Heretofore in this brief we have pointed out the clear distinction between the order of the New York Commission in the *New York Edison case* and Order No. 7–C with respect to the treatment of items after they are written into Account 100.4, which difference makes the decision of the New York court, referred to, inapplicable here.

With respect to the action of the Interstate Commerce Commission, it may fairly be said that the experience of that Commission in regulation has been principally in the railroad field, notwithstanding that telephone companies were within its jurisdiction for many years prior to the creation of the Federal Communications Commission. The Interstate Commerce Commission accordingly has not dealt with telephone rate cases; and in railroad rate cases it has not been confronted with excessive

or questionable claims for depreciation expenses, because the carriers have instituted depreciation accounting only for a small part of their depreciable property, and in the regulation of railroad rates the question of the rate base, and the question of operating expenses, have been less important and decisive than in public utility cases, where operations of single companies have been dealt with.

Under these circumstances, it is, perhaps, not strange that the Interstate Commerce Commission did not at once, and after brief argument before a single commissioner, appreciate the necessity for the original cost provisions which were then urged by the State commissions.

Seemingly counsel for the appellants consider that the failure of the Interstate Commerce Commission to adopt these original cost provisions is entitled to weight. If that be true, then we urge that the judgment of 22 State commissions, which at that time urged the provisions as reasonable and necessary, and the action of the State commissions which have since adopted the same provisions for purposes of State accounting, or through their National organization, have expressed approval of those provisions, is entitled to greater weight, for the reason that these commissions have had a greater experience with the difficulties which the provisions are designed to meet than the Interstate Commerce Commission has had.

No commissions have had longer or broader experience in public utility regulation than those of New York and Wisconsin. These commissions, as the citations in appellants' brief show, have adopted accounting regulations requiring the original cost of property, at the time when it was first dedicated to public use—whether incurred by the accounting company or by a predecessor company—to be recorded separately from all other costs. In this respect the accounting regulations of the two commissions just mentioned are identical with those of Order No. 7–C; and neither commission has modified such requirement.

In addition to the action taken by the Federal Communications Commission, in its order No. 7–C, and to the action of State commissions, above mentioned, we may cite the accounting order of the Federal Power Commission promulgated June 16, 1936, effective January 1, 1937, prescribing a uniform system of accounts for public utilities and licensees subject to the provisions of the Federal Power Act, analogous provisions of which are set out in the margin.[2]

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[2] "Definitions—When used in this system of accounts: (p. 4) * * *

"29. "Original cost", as applied to electric plant, means the cost of such property to the person first devoting it to public service (p. 6).

"100.1 Electric Plant in Service.

"A. This account shall include the original cost of electric plant included in accounts 301 to 390, together with the amounts recorded in accounts 391, 392, and 393, owned and used by the utility in its electric utility operations, including

The action of these State and Federal Commissions indicates such a consensus of opinion as to the original cost provisions involved as would seem

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such property owned by the utility but held by nominees. * * *

"100.2 Electric Plant Leased to Others.

"A. This account shall include the original cost of electric plant owned by the utility, but leased to others as operating units or systems where the lessee has exclusive possession. * * *

"100.3 Construction Work in Progress.

"This account shall include the total of the balances of work orders for electric plant in process of construction but not ready for service at the date of the balance sheet. * * *

"100.4 Electric Plant Held for Future Use.

"A. This account shall include the original cost of electric plant owned and held for use in electric service under a definite plan for such use. * * *

"100.5 Electric Plant Acquisition Adjustments.

"A. This account shall include the difference between (a) the cost to the accounting utility of electric plant acquired as an operating unit or system by purchase, merger, consolidation, liquidation, or otherwise, and (b) the original cost, estimated if not known, of such property, less the amount or amounts credited to the depreciation and amortization reserves of the accounting utility at the time of acquisition with respect to such property. The account shall be so subdivided as to show the amounts applicable to electric plant in service, electric plant leased to others, and electric plant held for future use. (See Electric plant instructions 2, 3, and 4.)

"B. Whenever practicable, this account shall be subdivided according to the character of the amounts included herein.

"C. Whenever practicable, a record shall be kept of the amounts in this account for each property acquisition.

"D. The amounts recorded in this account with respect to each property acquisition, shall be depreciated, amortized, or otherwise disposed of, as the Commission may approve or direct" (pp. 18–19).

to insure those provisions against the contention that they are unnecessary, unreasonable, or arbitrary.

It may be pointed out that, acting under a grant of power similar to Section 220 (a), the Interstate Commerce Commission has for a long period of time made particular orders based upon facts of particular cases. This was done in *Kansas City South Railway* v. *United States,* 231 U. S. 423, in *Norfolk and Western Railway* v. *United States,* 287 U. S. 134, in *Atlanta, Birmingham and Coast Railroad* v. *United States,* 296 U. S. 33, and in *Chesapeake & O. Ry.* v. *United States,* 5 Fed. Suppl. 7.

In *Kansas City Southern Railway* v. *United States,* the contention of the carrier, as stated by this court in its opinion, was—

> * * * that the power conferred upon the Commission to prescribe the forms of accounts, records, and memoranda to be kept by the carriers, recognizes a distinction between the form and the substance; and that while the Commission, in order to obtain full and accurate information concerning the affairs of each corporation, must have power to require any reports, schedules, and accounts necessary to show the true financial condition of each carrier; yet that the grant must by fair interpretation, and in order not to amount to an unconstitutional delegation of legislative power, stop short of the point where the regulation in its essence goes not

> to the form, but to the substance, and involves interference with the internal affairs of the corporation (231 U. S. 423, 440).

Disposing of this contention, the court declared the true object of the regulation provided for, and the necessity that the Commission's power should cover "substance" as included within a "form."

Its regulation must be such, the court said, as to make the accounts "speak a common language", so that the accounts for each company shall "display the pertinent financial operations of the company and throw light upon its present condition." The following is from the opinion of the court:

> We do not, however, think that any such distinction between the form and the substance is admissible with respect to the declared object of standardizing railroad accounts and obtaining therefrom full and accurate information concerning the affairs of the respective corporations. *The very object of a system of accounts is to display the pertinent financial operations of the company, and throw light upon its present condition. If they are to truly do this, the form must correspond with the substance.* * * *
>
> Plainly, the lawmaking body recognized the essential distinctions between property accounts and operating accounts, between capital and earnings; it recognized that the practice of different carriers varied in respect to these matters; and that no system of supervision and regulation would be com-

> plete without requiring the accounts of all the carriers to speak a common language.
>
> There is here no unconstitutional delegation of legislative powers. The reasoning adopted in *Interstate Commerce Commission* v. *Goodrich Transit Co.*, 224 U. S. 194, 210, etc., 56 L. ed. 729, 735, 32 Sup. Ct. Rep. 436, is controlling. And since, as just shown, uniformity in accounting is dependent upon the adoption and enforcement of precise classification, the authority to define the terms of the classification necessarily follows. It amounts, after all, to no more than laying down the general rules of action under which the Commission shall proceed, and *leaving it to the Commission to apply those rules to particular situations and circumstances by the establishment and enforcement of administrative regulations* (231 U. S. 423, 440–443). [Italics ours.]

Thus, in this early case, this court recognized the necessity which would require the making of administrative orders, based upon particular facts and circumstances and addressed to particular carriers.

Discussing the charging of the construction cost of the abandoned roadway, the court said:

> *Whether it should be charged against the accumulated profits* of previous years, as reflected in the Profit and Loss Accounts, *or against the profits of present and future years, may depend upon circumstances.* The theory upon which the Commission has

> acted in formulating its regulations is fairly stated in its brief herein as follows: * * * *In case, however, the amount is so large that its inclusion in a carrier's operating expenses for a single year would unduly burden the operating expense account for that year, the carrier may, if so authorized by the Commission, distribute the cost throughout a series of years.* [Italics supplied.]
>
> A statement of the theory is sufficient to show that the regulation is not arbitrary in the sense of being without reasonable basis. And there is evidence to show that the Commission was warranted in adopting it, as sustained by expert opinion and approved by experience (231 U. S. 423, 451–452).

This discussion clearly shows that the Commission was exercising the power to make particular orders at that early time, and that the court approved that practice.

In *Norfolk and Western Railroad* v. *United States,* 287 U. S. 134, the court dealt with a case where the Commission had entertained a petition by the plaintiff carrier asking for an order permitting it to transfer certain coal lands, used exclusively for the production of coal for locomotive use upon the petitioner's road, from an account which covered non-carrier property to an account which covered investment in road and equipment. The Commission denied the petition, and made an order directing the accounting to be performed. The carrier sought to enjoin enforcement of the order.

Examining the origin and purpose of the statutory provisions giving the Commission power to prescribe accounts and the practice of the Commission thereunder, the court sustained the Commission's order, *and it did this upon the ground that whether a special classification order should be made to fit a particular case was within the discretion conferred upon the Commission.* We quote what the court said on this point:

> Plainly, the Commission, under the authority conferred upon it by Congress, must draw a line between the two sorts of property owned by the railroads. Within broad limits that body's determination is necessarily beyond revision and correction by the courts. The record shows that it is unusual for a railroad to own mines for the production of locomotive fuel; in fact we are referred to no other similar instance. *Whether the Commission should make special classifications to fit exceptional cases lies within the discretion conferred,* and courts ought not to be called upon to interfere with or correct alleged errors with respect to accounting practice. If we were in disagreement with the Commission as to the wisdom and propriety of the order, we are without power to usurp its discretion and substitute our own (287 U. S. 134, 141). [Italics ours.]

After the Interstate Commerce Commission had for many years interpreted the identical language of Section 220 (a) in the Interstate Commerce Act, herein before quoted, as giving that Commission

power to make particular orders, the reenactment of that language in the Communications Act without change constituted legislative approval of the construction theretofore placed upon it.

There is nothing novel in the requirement that the cost of property shall be divided and recorded in different accounts. The accounting system prescribed by the Interstate Commerce Commission and now in effect, which the appellants approve, and desire to retain, provides for such division, but with much less precision, and with correspondingly less informing results than the system prescribed by Order No. 7–C. The court below in its opinion very clearly stated and contrasted the requirements of the two systems (R. 566–568).

Furthermore it should be noted that the Interstate Commerce Commission's system of accounts provides for particular orders of the Commission addressed to particular companies. Such administrative orders are contemplated by paragraph (D), (E), and (F) of Instruction 21 (R. 366).

The requirement of the Commission's order, contained in Instruction 2 (B1) that "all charges to the accounts prescribed in the classification for telephone plant, income, operating revenues, and operating expenses shall be just and reasonable and any payments by the company in excess of such just and reasonable charges shall be included in Account 323, 'Miscellaneous income charges'" is not arbitrary or unreasonable, nor beyond the authority of the Commission nor violative of the due process clause of the Fifth Amendment

Concerning this instruction, the court below said:

"The information this requirement makes available is essential to any determination of reasonable rates within 201 (b) of the Act (ch. 1 (4–5) of the Interstate Commerce Act) since they are directly affected by such charges. In the present system, instruction 22 (10) (a) stipulates that the telephone plant accounts be charged with "reasonable amounts for interest during construction period." The concept is no more definite there than the one more widely applied in the proposed system. The idea of "reasonable" is old in the fixation of public utility rates and every rate determination involves consideration of charges here made subject to a distinction between reasonable and unreasonable. Although in isolated cases the question may be very close, generally the classification will not be impossible. As an accounting measure merely, the rule cannot be regarded as beyond the Commission's power.

"Exception is also taken to the rule as requiring obedience to a standard as vague and indefinite as to be unconstitutional within the doctrine announced in *United States* v. *Cohen Grocery* (255 U. S. 81), *Tedrow* v. *Lewis & Son Co.* (255 U. S. 98) and *A. B. Small Co.* v. *American Sugar Refining Co.* (267 U. S. 233). First, it appears that the requirement that profits on transactions involving necessaries should not be unjust or unreasonable is without the specialized content of the word "reasonable" with regard to charges involved in the de-

termination of rates. This serves to distinguish the plaintiff's other cases. cf. *Connelly* v. *General Construction Co.,* 264 U. S. 385; *Cline* v. *Trink Dairy Co.,* 274 U. S. 445; *Champlin Refining Co.* v. *Oklahoma Corp. Commission,* 286 U. S. 210.

"Second, telephone companies need incur no risk since those occasional cases which may be doubtful can be submitted for approval under Sec. 220 (g) of the act and instruction 9 of the order. To the claim that the Commission is likewise without a standard for judgment, the answer is that the concept of "reasonable" is traditionally defined in utility regulation with sufficient certainty.

"The necessity of this order becomes apparent upon consideration of the interrelations of telephone companies. License agreements between subsidiaries can furnish examples of charges clearly not "just and reasonable." Yet any exact definition would be objectionable as arbitrary.

"Furthermore, these items, in being subject to interpretation by the Commission and definition as applied to specific facts, are sufficiently definite to guide the Commission. Cf. *Pennsylvania Co.* v. *United States,* 236 U. S. 351, 361; *Interstate Commerce Commission* v. *Alabama Midland Ry.,* 168 U. S. 144, 170 (R. 570).

Criticism of the instruction is based upon a misconception of the law which we have already discussed. Appellants construe the Communica-

tions Act as granting to the Commission power to regulate accounts only by the promulgation of general accounting rules and regulations, and not by the making of orders addressed to particular companies dealing with particular matters. This is a misconception, as has been already pointed out.

Congress, in the act, has laid down the general rule of uniformity, leaving it to the Commission to apply that rule "to particular situations and circumstances by the establishment and enforcement of administrative regulations."

For the Commission's constant use in the regulation of rates, as we have before pointed out, the Commission must know approximately as to each utility subject to its jurisdiction, not only the approximate value of the property of the utility, but its operating revenues, and its just and reasonable operating expenditures. The Commission has, accordingly, laid down the general rules that all charges to the accounts mentioned in instruction 2b (1) shall be just and reasonable. Amounts received or disbursed in the usual course and upon ordinary considerations will fall within the description of the classification. The isolated case should be presented to the Commission for its direction. In no other manner can unreasonable disbursements be kept out of the capital accounts and the operating expense accounts.

In an early case before this court, involving the power of the Interstate Commerce Commission to

regulate accounts, this power on the part of the Commission to apply general rules to the particular facts of particular situations was clearly recognized. The court said:

> * * * And since, * * *, uniformity in accounting is dependent upon the adoption and enforcement of precise classification, the authority to define the terms of the classification necessarily follows. It amounts, after all, to no more than laying down the general rules of action under which the Commission shall proceed, and leaving it to the Commission to apply those rules to particular situations and circumstances by the establishment and enforcement of administrative regulations. *Kansas City Southern Railway Co.* v. *United States et al.*, 231 U. S. 423, 443.

The instructions contained in said order No. 7-C with respect to what property shall be entered in Accounts 100.1, 100.3, and 103 do not deprive the appellants of their rights under the due process clause of the fifth amendment

These instructions are as follows:

> *100.1. Telephone plant service.*—This account shall include the original cost (note instruction 3–S–1) of the company's property used in telephone service at the date of the balance-sheet as classified under accounts 201 to 277, inclusive (note instructions 3–AA, 20, and 21)" (R. 122).
>
> *100.3 Property held for future telephone use.*—(A) This account shall include the

original cost (note instruction 3–S. 1) of property owned and held for imminent use in telephone service under a definite plan for such use * * * (R. 123).

103. Miscellaneous physical property.— This account shall include the company's investment in physical property other than property the investment in which is includible in accounts 100.1, "Telephone plant in service"; 100.2, "Telephone plant under construction"; and 100.3, "Property held for future telephone use." It shall include the company's investment in telephone property retired (note instruction 3–T) and held for sale; and also property such as lighting, water, power, and manufacturing plants not held incident to the company's telephone operations, and assessments against miscellaneous physical property for the construction of public improvements (R. 125).

The appellants base their contention that these instructions are unconstitutional upon the assertion that they are vague and arbitrary, made by the accounting experts whose affidavits the appellants presented to the court below. We will notice these affidavits briefly.

Affiant Sangster criticised the quoted directions because, as he asserts, they lack definitions of the practical meaning of the terms "property used in telephone service" and "property held for imminent use", and because, as he also asserted, uncertainty may exist whether property purchased for future use should be charged to account 100.3 or to

account 103 (R. 314–315). The affiant Madden especially criticised the use of the term "imminent", which he says "has no particular significance, insofar as accounting terminology is concerned" (R. 322). Likewise he considered that the words "used in telephone service" and "held for imminent use" put an "intolerable burden upon the accountants" (R. 323). The affiant Kester expressed the opinion that those terms are "too vague to distinguish adequately the one from the other, accountants would not know definitely to what account plant should be charged, and there would be bound to be variation of opinion which would be destructive of uniformity" (R. 329–330). The affiant Heis made substantially the same character of criticism (R. 343–344).

The affiant Young expressed the view that provisions of the order would require a change in the classification of cable laid in the street every time a subscriber discontinued a telephone and thus made a part of the cable idle property.

It is impossible to read the several affidavits touching this matter with their substantially identical expressions without reaching the conclusion that the opinions expressed are largely based upon these fanciful assumptions of Mr. Young.

In response to these prognostications of difficulty to be encountered in complying with the order, the Commission's Chief Accountant, Mr. Norfleet, formerly Chief Accountant of the Interstate Com-

merce Commission, speaking on the basis of experience of seventeen years with that Commission, said:

> 1. There is nothing in the accounting system prescribed by this Commission to justify the statement of plaintiffs that the dividing lines between Accounts 100.1, "Telephone plant in service"; 100.3, "Property held for future telephone use"; and 103, "Miscellaneous physical property", are so indefinite and ambiguous that it would be impossible for plaintiffs to know to which account substantial amounts of their property should be charged.
>
> 2. The nature of the properties to be recorded in these respective accounts are specifically set forth in the text thereof. (See pages 26, 27, 28, and 29 of the Uniform System of Accounts prescribed by this Commission.)
>
> 3. There may develop so-called borderline cases calling for interpretations of the pertinent accounting regulations. This is true with respect to the provisions of any system of accounts which, in general terms, must cover a broad field of activities and has been and is true of the system of accounts prescribed by the Interstate Commerce Commission which plaintiffs seek to retain. A familiar illustration of the necessity for such interpretations, known to all persons familiar with accounting, is the distinction between capital and revenue expenditures. The problem of differentiating between entries to be made in Accounts 100.1,

100.3, and 103 here discussed, is, in my opinion, comparatively simple and amply provided for by the explicit instructions contained in this Commission's system of accounts.

4. In the event that plaintiffs or other telephone companies may desire assistance or advice of this Commission in classifying any item to be recorded in their accounts, they may submit all questions of doubtful interpretation of prescribed accounting to this commission for consideration and decision as provided in instruction 9 of this Commission's system of accounts. For more than twenty years it has been the common practice of plaintiffs and other telephone companies to follow this procedure in submitting to the Interstate Commerce Commission or this Commission numerous inquiries requesting such interpretations relating to accounting regulations.

5. It is significant that the plaintiffs have submitted no inquiries to this Commission with reference to an interpretation of the above accounts. In view of the facts mentioned in the next preceding paragraph, there is no reasonable basis for any accounting official of plaintiffs to conclude or believe that they will be required to make any accounting entry "at their peril" by reason of this Commission's system of accounts. To the contrary, they have every reason to believe that this Commission will lend all needful assistance in the practical and reasonable application of its accounting regulations.

6. The language used in the text of the accounts above complained of is and has been long in use and understood in the public utility field by those professionally interested in these matters and, in my opinion, is neither contrary to fundamental practice of accounting, arbitrary, nor unreasonable.

DEPRECIATION OF SPARE PLANT

* * * 3. It is my opinion and understanding that this Commission's system of accounts permits the recording of necessary "stand-by" plant in Account 100.1, "Telephone plant in service" and that periodical transfers between said Account 100.1 and Account 100.3, "Property held for future telephone use" will not be required by reason of seasonable changes or fluctuating demands for plaintiffs' services. It is also my understanding that such interpretation was discussed and made clear at the conference between representatives of this Commission and representatives of plaintiffs and other telephone companies relating to the then proposed system of accounts for telephone companies, on May 16, 1935 (R. 480–481).

Other evidence before the court below touching this matter will be found in the affidavits following: Bickley (R. 509–510); Colbert (R. 528–529); Orton (537–538), Smith (R. 549).

Referring to an interpretation of Account 100.1, made by the Wisconsin Commission, and set out

at page 47 of their brief, the appellants make the following statement:

> Such a clarification of Account 100.1 would satisfy appellants, but we have no assurance it will be so interpreted, because, though requested (R. 555–6) the Communications Commission has refused to modify or clarify the definition.

If the portion of the record cited by appellants is referred to, it will be seen that the accountants of the Federal Communications Commission have consistently interpreted Account 100.1 as it was interpreted by the Wisconsin Commission. The Complaint of the appellants as to that account comes seemingly to this; that phraseology deemed desirable by appellants' accountant Heiss was not considered necessary to make clear an interpretation of Account 100.1, which the appellants desire, and the Federal Communications Commission, through its Chief Accountant, says the account was designed to have.

In this connection we point out that the appellants did not seek to perfect the accounting system prescribed by a motion for rehearing, similar to that whereby clarification of the Wisconsin order was obtained, although such a motion is expressly authorized by Section 5 (c) of the Communications Act, and would have insured to the appellants a review of the provisions of this accounting order, not only by the members of the Telephone Division, but by the seven members of the full Commission.

Order No. 7–C was issued June 19, 1935, not to become effective until January 1, 1936. Abundant time was available for seeking to correct any defects in the order by a motion for a rehearing. Such a motion should have been filed before the institution of this action. *United States* v. *Abilene and Southern Railway Company,* 265 U. S. 274, 282.

The affidavits presented on behalf of the Commission fully sustained finding XV of the court below, which is as follows:

> The distinctions between Accounts 100.1, 100.3, and 103, and the respective amounts includible therein, are sufficiently clear and definite from the titles and texts of the accounts, and instructions relating thereto, to be understood readily by those charged with the duty of keeping said accounts (R. 576).

The provisions of Order No. 7–C challenged by the appellants are severable from the other provisions of said order, and the validity of the order, as a whole, does not depend upon the validity of those provisions

The court below found as follows:

XVIII

> Telephone Division Order No. 7–C constitutes a complete system of accounts for telephone companies but the provisions therein complained of are separable (R. 577).

The evidence supporting this finding is in the following affidavits: Nortleet paragraph VII (R.

483); Rains, paragraph 25, (R. 492); Orton, paragraph 8 (R. 542).

The statement of Mr. Orton, who is Director of Research and valuation of the Public Service Commission of New York, is as follows:

> 8. ARE PROVISIONS OBJECTED TO NON-SEVERABLE FROM REMAINDER OF THE SYSTEM?
>
> It is alleged in the Bills of Complaint and contended in all of the affidavits that the provisions objected to are non-severable and that they are inter-dependent with the other provisions of the system of accounts, and that if they are eliminated there is left an incomplete system under which it would be impracticable to keep proper books of account. This contention is sound only upon the legal theory that if the provisions of any account with reference to certain classes of property or transactions are found invalid they are eliminated and nothing is or can be put in their place regarding such property or transaction, thus leaving an absolute blank in the system of accounts in these respects. Obviously if such is the case the system is incomplete and impossible of application if any account is eliminated. As a practical accounting matter, however, it is not, in my opinion, at all necessary that this should be the case. The complainants' objections are limited to a few specific accounts, and it would be entirely feasible, even if such objections were sustained, either temporarily, pending further investigation,

> or permanently to substitute in regard to such accounts the accounting procedure contended for by the complainants, but leave in full effect the prescribed system of accounts in regard to all other matters. Whether this can be done as a matter of law, I do not profess to express an opinion, but as a matter of practical accounting I see no difficulty whatsoever (R. 542).

The evidence upon which the appellants rely will be found in the following affidavits presented by them: Sangster, paragraph IX, R. 316; Madden, paragraph VI (R. 323); Kester, paragraph 6 (R. 330); and Heis (R. 344).

Affiant Madden stated as follows:

> VI. SYSTEM INCOMPLETE WITHOUT PROVISIONS CRITICISED.
>
> If the provisions of the system of accounts which I have characterized as unsound or contrary to sound principles of correct accounting were removed from the system, it would not be a complete system of accounts. Essential parts would be missing and unless substitute provisions were written in to take their places it would be impossible to keep a set of accounts in accordance with the system (R. 323).

Affiant Kester's statement is in the same identical words as this statement of affiant Madden, and the statements of the two other affiants are substantially the same.

These affidavits, as will be seen, go only to the point of asserting that if the provisions criticised

by the affiants are removed from the system the system will not be complete. This is quite obvious, but it is far from supporting the assertion that the remainder of the system can not be followed, leaving the invalidated provisions ineffective, and the accounting of the appellants to be made in accordance with such parts of the accounting system now in force, as are left operative by the excission of the parts of Order No. 7–C which may be condemned, if any.

Respectfully submitted.

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U. S. GOVERNMENT PRINTING OFFICE: 1936

In the Supreme Court of the United States

OCTOBER TERM, 1936

No. 74

AMERICAN TELEPHONE AND TELEGRAPH CO. ET AL., APPELLANTS

v.

THE UNITED STATES OF AMERICA, FEDERAL COMMUNICATIONS COMMISSION, AND NATIONAL ASSOCIATION OF RAILROAD AND UTILITIES COMMISSIONERS

ON APPEAL FROM THE DISTRICT COURT OF THE UNITED STATES FOR THE SOUTHERN DISTRICT OF NEW YORK

SUPPLEMENTAL MEMORANDUM BY THE UNITED STATES AND THE FEDERAL COMMUNICATIONS COMMISSION

The Federal Communications Commission construes the provisions of Telephone Division Order No. 7–C, issued June 19, 1935, pertaining to account 100.4, as follows:

(1) That amounts included in account 100.4 that are deemed, after a fair consideration of all the circumstances, to represent an investment which the accounting company has made in assets of con-

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tinuing value will be retained in that account until such assets cease to exist or are retired; and, in accordance with paragraph (C) of account 100.4, provision will be made for their amortization.

(2) That when amounts included in account 100.4 are deemed, after a fair consideration of all the circumstances, to be definitely attributable to depreciable telephone plant, provision will be made for amortization of such amounts through operating expenses, through the medium of either account 613 (R. 186) or account 675 (R. 205).

The Commission believes that the foregoing construction of its order is that which it presented to the District Court through the affidavits of its witnesses.

Respectfully submitted.

STANLEY REED,
Solicitor General.
JOHN DICKINSON,
Assistant Attorney General.
HAMPSON GARY,
General Counsel,
Federal Communications Commission.

NOVEMBER 1936.

U. S. GOVERNMENT PRINTING OFFICE: 1936

SUPREME COURT OF THE UNITED STATES.

No. 74.—October Term, 1936.

American Telephone & Telegraph Company, et al., Appellants, *vs.* The United States of America, Federal Communications Commission, and National Association of Railroad and Utilities Commissioners.	Appeal from the District Court of the United States for the Southern District of New York.

[December 7, 1936.]

Mr Justice Cardozo delivered the opinion of the Court.

This suit was brought in the United States District Court for the Southern District of New York to set aside an order of the Federal Communications Commission prescribing a uniform system of accounts for telephone companies subject to the Communications Act of 1934. Act of June 19, 1934, c. 652; 48 Stat. 1064; 47 U. S. C. sec. 151. The plaintiffs are forty-four telephone companies, thirty-seven of them members of the Bell system, and seven of them members of another group. The defendants are the United States and the Federal Communications Commission, with whom the National Association of Railroad and Utilities Commissioners was afterwards joined, intervening as the representative of the regulatory commissions of forty-six states in support of the contested order.

The Communications Act of 1934 provides (sec. 220) that "the Commission may, in its discretion, prescribe the forms of any and all accounts, records, and memoranda" to be kept by carriers subject to the Act, "including the accounts, records, and memoranda of the movement of traffic, as well as of the receipts and expenditures of moneys". This is a power that had previously been lodged with the Interstate Commerce Commission (Interstate Commerce Act, sec. 20 (5)), which framed a set of rules for telephone companies to take effect January 1, 1913, and a revised set of rules effective January 1, 1933. After the transfer of jurisdiction over telephone companies from the Interstate Commerce Commission to the Federal Communications Commission in 1934, the new Commission prepared a "draft of a Uniform System of Accounts",

which was considered at a conference with representatives of the companies and of the state commissions. The outcome of the conference was the order of June 19, 1935, to take effect January 1, 1936, which is the subject of this suit.

The plaintiffs having moved for an interlocutory injunction, the cause was heard, in accordance with the requirement of the statute (47 U. S. C. sec. 402 (a); 28 U. S. C. sec. 47) by a District Court of three judges, the affidavits in support of the motion and against it being also submitted for and against the final decree. Five provisions of the order were attacked as arbitrary. The District Court sustained two objections of minor importance, which are not in controversy now, and overruled the others. One of these was directed to the "original cost" rule; the second to a provision as to "just and reasonable" charges; the third to a classification dividing plants in present use from those held for use thereafter. The court dismissed the bill as to the objections overruled, stating in an opinion the reasons for its action. 14 F. Supp. 121. The case is here upon appeal. 48 Stat. 1064, 1093, sec. 402 (a); 47 U. S. C. sec. 402 (a); 38 Stat. 219, 220; 28 U. S. C. secs. 47, 47 (a).

This court is not at liberty to substitute its own discretion for that of administrative officers who have kept within the bounds of their administrative powers. To show that these have been exceeded in the field of action here involved, it is not enough that the prescribed system of accounts shall appear to be unwise or burdensome or inferior to another. Error or unwisdom is not equivalent to abuse. What has been ordered must appear to be "so entirely at odds with fundamental principles of correct accounting" (*Kansas City Southern Ry. Co.* v. *United States,* 231 U. S. 423, 444) as to be the expression of a whim rather than an exercise of judgment. *Norfolk & Western Ry. Co.* v. *United States,* 287 U. S. 134, 141; *Kansas City Southern Ry. Co.* v. *United States, supra,* p. 456. Then too, in gauging rationality, regard must steadily be had to the ends that a uniform system of accounts is intended to promote. "The object of requiring such accounts to be kept in a uniform way and to be open to the inspection of the Commission is not to enable it to regulate the affairs of the corporations not within its jurisdiction, but to be informed concerning the business methods of the corporations subject to the act that it may properly regulate such matters as are really within its jurisdiction." *Interstate Commerce Commission* v. *Goodrich Transit Co.,* 224 U. S. 194,

211; *cf. Kansas City Southern Ry. Co.* v. *United States, supra,* p. 445. With these principles in mind, we proceed to consider separately the regulations and instructions now challenged as unlawful.

First: *The Original Cost Provisions.*

Four new balance sheet accounts, each of them a sub-title of the general title of "Investments", must be kept under the new system. The first (100.1) is described as Telephone Plant in Service; the second (100.2), Telephone Plant under Construction; the third (100.3), Property held for Future Telephone Use; and the fourth (100.4), Telephone Plant Acquisition Adjustment. Account 100.1 "shall include the original cost [defined by Instruction 3 (S. 1)] of the company's property used in telephone service at the date of the balance sheet". Account 100.2 "shall include the original cost [as so defined] of construction of telephone plant not completed ready for service" at such date. Account 100.3 "shall include the original cost [so defined] of property owned and held for imminent use in telephone service under a definite plan for such use." The term "original cost" as appearing in these rules receives (under Instruction 3 (S. 1)) a special definition. " 'Original cost' or 'cost', as applied to telephone plant, franchises, patent rights, and right-of-way, means the actual money cost of (or the current money value of any consideration other than money exchanged for) property at the time when it was first dedicated to the public use, whether by the accounting company or by a predecessor public utility." If actual costs are unknown, estimates are to take their place. Instruction 21 (B). From all this it follows that the sum of the three accounts which represent the original cost of property acquired by the accounting company from other telephone utilities, may be less or greater than the investment in such property by the accounting company itself. The difference is taken care of by account 100.4, Telephone Plant Acquisition Adjustment.* The same rule provides in a subdivision designated (C)

*"'This account shall include the difference between (a) the amount of money actually paid (or the current money value of any consideration other than money exchanged) for telephone plant acquired, plus preliminary expenses incurred in connection with the acquisition; and (b) the original cost (note instruction 3 (S. 1)) of such plant, governmental franchises and similar rights acquired, less the amounts of reserve requirements for depreciation and amortization of the property acquired, and amounts of contributions to the predecessor company or companies for construction and acquisition of such property. If the actual original cost is not known, the entries in this account shall be based upon an estimate of such cost."

that "the amounts recorded in this account [i. e. 100.4] with respect to each property acquisition shall be disposed of, written off, or provision shall be made for the amortization thereof in such manner as this Commission may direct".

Before explaining the appellants' objections to these provisions as to cost, we may pause to indicate the reasons that led to their adoption. To a great extent, the telephone business as conducted in the United States is that of a far flung system of parent, subsidiary and affiliated companies. The Bell system is represented in this case by thirty-seven companies, the American Telephone and Telegraph Company at their head. Seven other companies, intervening as a group, represent a second and smaller system. Purchases are frequently made by a member or members of a system from affiliates or subsidiaries, and with comparative infrequency from strangers. At times obscurity or confusion has been born of such relations. There is widespread belief that transfers between affiliates or subsidiaries complicate the task of rate-making for regulatory commissions and impede the search for truth. Buyer and seller in such circumstances may not be dealing at arm's length, and the price agreed upon between them may be a poor criterion of value. *Dayton Power & Light Co.* v. *Public Utilities Comm. of Ohio,* 292 U. S. 290, 295; *Western Distributing Co.* v. *Public Service Comm. of Kansas,* 285 U. S. 119; *Smith* v. *Illinois Bell Telephone Co.,* 282 U. S. 133. Even if the property has been acquired by treaty with an independent utility or a member of a rival system, there is always a possibility that it is nuisance value only—and not market or intrinsic value for the uses of the business—that has dictated the price paid. Accordingly the work of the Commission may be facilitated by spreading on the face of the accounts a statement of the cost as of the time when the property to be valued was first acquired by a utility or dedicated to the public use. The same considerations show why the regulations do not direct that the inquiry as to original cost shall be carried even farther back, so as to cover, for illustration, the cost to manufacturers who may have sold to the first utility. In the process of analysis, inquiry is halted at the point where it ceases to be fruitful.

With this explanatory background we can now go forward with understanding to a statement of the objections to the order and a determination of their weight.

(a) The companies object that by the "original cost" provisions of the order they are prevented "from recording their actual investment in their accounts" with the result that the accounts do not fairly exhibit their financial situation to shareholders, investors, tax collectors and others.

The argument is that account 100.4, representing the difference between original and present cost, is not to be reckoned, either wholly or in part, as a statement of existing assets, but must be written off completely. The Commission is charged, we are told, with a mandatory duty to extinguish the entire balance recorded in that account, its presence under the title of "investments" having the effect of a misleading label. To give support to that conception of official duty, they rely on subdivision (C), which provides, as we have seen, that "the amounts recorded in this account with respect to each property acquisition shall be disposed of, written off, or provision shall be made for the amortization thereof in such manner as this Commission may direct."

If subdivision (C) had the meaning thus imputed to it, there would be force in the contention that the effect of the order is to distort in an arbitrary fashion the value of the assets. But the imputed meaning is not the true one. The Commission is not under a duty to write off the whole or any part of the balance in 100.4, if the difference between original and present cost is a true increment of value. On the contrary, only such amount will be written off as appears, upon an application for appropriate directions, to be a fictitious or paper increment. This is made clear, if it might otherwise be doubtful, by administrative construction. Thus, the Commission's chief-accountant testified that by the proper interpretation of account 100.4, amounts therein "would be disposed of, after the character of the item had been determined, in a manner consistent with the general rules underlying the uniform system of accounts for the distribution of expenditures, according to their character, to operating expenses, income, surplus, *or remain an investment.*" Other witnesses gave testimony in substance to the same effect. But even more decisive are statements made by counsel, appearing for the Government and arguing the case before us. To avoid the chance of misunderstanding and to give adequate assurance to the companies as to the practice to be followed, we requested the Assistant Attorney-General to reduce

his statements in that regard to writing in behalf of the Commission. He did this and informs us that "the Federal Communications Commission construes the provisions of Telephone Division Order No. 7-C, issued June 19, 1935, pertaining to account 100.4" as meaning "that amounts included in account 100.4 that are deemed, after a fair consideration of all the circumstances, to represent an investment which the accounting company has made in assets of continuing value will be retained in that account until such assets cease to exist or are retired; and, in accordance with paragraph (C) of account 100.4, provision will be made for their amortization."

We accept this declaration as an administrative construction binding upon the Commission in its future dealings with the companies. *Hicklin* v. *Coney*, 290 U. S. 169, 175; *Addy Co.* v. *United States*, 264 U. S. 239, 245. The case in that respect is sharply distinguished from *Matter of New York Edison Co.* v. *Maltbie*, 244 App. Div. (N. Y.) 685; 271 N. Y. 103, where under rules prescribed by the Public Service Commission of New York, there was an inflexible requirement that an account similar in some aspects to 100.4 be written off in its entirety out of surplus, whether the value there recorded was genuine or false. The administrative construction now affixed to the contested order devitalizes the objection that the difference between present value and original cost is withdrawn from recognition as a legitimate investment.

We are not impressed by the argument that the classification is to be viewed as arbitrary because the fate of any item, its ultimate disposition, remains in some degree uncertain until the Commission has given particular directions with reference thereto. By being included in the adjustment account, it is classified as provisionally a true investment, subject to be taken out of that account and given a different character if investigation by the Commission shows it to be deserving of that treatment. Such a reservation does not amount to a departure from the statutory power to fix the forms of accounts for "classes" of carriers rather than for individuals. The forms of the accounts *are* fixed, and fixed by regulations of adequate generality. What disposition of their content may afterwards be suitable upon discovery that particular items have been carried at an excessive figure must depend upon evidentiary circumstances, difficult to define or catalogue in advance

of the event. If once there was any need for explanation more precise than that afforded by the order, it is now supplied, we think, by an administrative construction, which must be read into the order as supplementary thereto.

(b) The companies object that by the provisions as to "original cost" they are prevented "from recovering depreciation expense, which they actually incur, on their actual investment", and are required "to base depreciation charges on the cost to a prior owner."

This objection, like the one last considered, has its origin in the belief that what is recorded in "telephone plant acquisition adjustment" must inevitably be written off, and is not subject to the treatment appropriate to genuine assets.

Here again the construction of the regulations by the Commission itself is enough to dispel the fear that in their practical operation they will become instruments of hardship. Without dwelling on the testimony, we content ourselves with a quotation from the statement filed by counsel at the conclusion of the argument. The Commission there informs us that "when amounts included in account 100.4 are deemed, after a fair consideration of all the circumstances, to be definitely attributable to depreciable telephone plant, provision will be made for amortization of such amounts through operating expenses, through the medium of either account 613 [which covers the amortization of intangible property] or account 675 [which includes all operating expenses not properly chargeable to other accounts]."

Obviously account 675 was inserted as a catch-all to cover previous omissions. We do not need to inquire whether under an ideal system of accounting the amounts to be amortized would be chargeable to an account entitled in some other way. It is enough that by the ruling of the Commission they will find a lodgement here, with an appropriate entry betokening their meaning. A system of accounts may be awkward or imperfect, and yet not so "arbitrary and outrageous" (*Norfolk & Western Ry. Co.* v. *United States, supra,* p. 143) as to justify a court in restraining its enforcement.

Appellants insist that amortization is an afterthought as applied to the account in controversy, and that there must be an amendment of the rules, if the Commission is to resort to such a process.

We read the record otherwise. In setting up the amortization reserve account (172), the rules expressly provide that "it shall also be credited with any amounts which the Commission may authorize under a plan to amortize the balance in account 100.4, Telephone Plant Acquisition Adjustment."

In the same connection, the point is made that section 220 (b) of the Act requires more specific directions as to depreciation or amortization than the Commission has supplied. By that section, "the Commission shall, as soon as practicable, prescribe . . . the classes of property for which depreciation charges may be properly included under operating expenses." No objection is made that the directions are not sufficiently specific as to account 100.1, Telephone Plant in Service. The objection is confined to account 100.4. But one of the very reasons for establishing that account is that in advance of inquiry by the Commission as to the property there included it is impracticable to determine what portion of it may properly be subjected to charges of this nature. When that inquiry has been completed, the Commission will be in possession of the necessary data. Provision will then be made for amortization of any amounts in the account that may properly be classified as investment in depreciable property. The label is unimportant, whether depreciation or amortization, if the substance of allowance is adequately preserved.

(c) The companies object that by the "original cost" provisions of the order they are required, where the actual cost is unknown, to record an estimate of cost, and that this requirement is an arbitrary one, mutilating their accounts and exposing them to the hazard of criminal prosecution.

What was ordered by the Commission in that behalf is expressly authorized by the statute with the result that to invalidate the order will be to invalidate the statute also. By section 213 (c) of the Communications Act of 1934 it is provided that "if any part of such cost cannot be determined from accounting or other records, the portion of the property for which such cost cannot be determined shall be reported to the Commission; and, if the Commission shall so direct, the original cost thereof shall be estimated in such manner as the Commission may prescribe."

In the vast majority of cases, original cost will be ascertainable from the records of the previous owners. If these have been lost or are not available or trustworthy, the order makes provision for

the substitution of an estimate. Difficulties in the making of such an estimate are indicated by the companies. We doubt whether in any instance they will be found to be insuperable, but if they shall ever prove to be so, means will be at hand whereby an avenue of escape from injustice will be opened without resort to the drastic remedy of declaring the order void. Estimates are at times inevitable in any system of accounts. Even under the system previously in vogue, the total purchase price, which was entered in an account known as "telephone plant", was subdivided into a series of accounts covering respectively pole lines, cable, aerial wire, and other classes, and distributed among them. If the price was a lump sum, there was need to resort to estimates in the process of subdivision. So, also, estimates were always necessary upon the retirement of plant or equipment acquired at varying dates, unless the articles retired were so clearly identified that the dates of acquisition and the prices then paid for each of them were susceptible of ascertainment upon the face of the accounts themselves. All that can be said of the present regulations is that they make the occasion for estimates more frequent than in former years and the process more involved. The difference in degree is not proved to be so great as to drag nullity in its train. If instances shall occur in which a company is unable to make an intelligent estimate with even approximate correctness, that exceptional event will justify resort to the Commission for particular instructions. In no event is there a substantial hazard of criminal prosecution. To subject the company or its officers to prosecution for a crime the violation of the Act must have been knowing and wilful. Communications Act of 1934, secs. 501, 502; *Hygrade Provision Co.* v. *Sherman*, 266 U. S. 497, 502, 503; *United States* v. *Murdock*, 290 U. S. 389. Penalties do not follow upon innocent mistakes.

(d) The companies object also that even when property recorded in the adjustment account (100.4) is recognized by the Commission as a continuing investment, there will be difficulty in determining the amount to be written out of that account when the property is withdrawn. No reason is apparent why this difficulty should be any greater than it would be if the same property had been recorded in a single plant account without separation of the original cost from the cost at later dates. However that may be, there is ample provision in the rules for clarifying instructions whenever duty is uncertain.

Second: *The provisions for just and reasonable charges.*

The companies object to the following instructions (described as 2 (B. 1)): "All charges to the accounts prescribed in this classification for telephone plant, income, operating revenues, and operating expenses shall be just and reasonable and any payments by the company in excess of such just and reasonable charges shall be included in account 323, 'Miscellaneous income charges.'"

The purpose of this requirement is to prevent the padding of the accounts by charges knowingly and wilfully entered in excess of what is just and reasonable. Only if knowingly and wilfully so entered is any penalty prescribed therefor. *United States* v. *Murdock, supra.* There is surely nothing arbitrary in establishing a standard of behavior so consistent with good morals. On the contrary, the need for such a standard has been made manifest for years as the result of intercorporate relations that are matters of common knowledge. *Dayton Power & Light Co.* v. *Public Utlities Comm. of Ohio, supra; Lindheimer* v. *Illinois Bell Telephone Co.,* 292 U. S. 151. "The Commission must have power to prevent evasion of its orders and detect in any formal compliance or in the assignment of expenses a 'possible concealment of forbidden practices.'" *Smith* v. *Interstate Commerce Commission,* 245 U. S. 33, 45. In such a context the standard of the "just and reasonable" is not unduly vague. *Nash* v. *United States,* 229 U. S. 373, 377; *International Harvester Co.* v. *Kentucky,* 234 U. S. 216, 223; *United States* v. *Cohen Grocery Co.,* 255 U. S. 81, 92; *United States* v. *Wurzbach,* 280 U. S. 396, 399; *People* v. *Mancuso,* 255 N. Y. 463, 470. "Moreover . . . since the statutes require a specific intent to defraud in order to encounter their prohibitions, the hazard of prosecution which appellants fear loses whatever substantial foundation it might have in the absence of such a requirement." *Hygrade Provision Co.* v. *Sherman, supra.*

Third: *The classification of plant as used in present service or held for use thereafter.*

Property "used in telephone service at the date of the balance-sheet" goes into account 100.1; property "held for imminent use in telephone service" under a definite plan for such use goes into account 100.3; and other property held for future use not imminent or definite goes into still another account, 103, which covers "miscellaneous physical property."

The companies object that this classification is so vague as to be arbitrary. We do not look at it that way. Property held for imminent use in telephone service and under a definite plan will include spare plants kept in reserve as a measure of prudent administration. Such uses had consideration by this court in a recent opinion. *Columbus Gas & Fuel Co.* v. *Public Utilities Comm. of Ohio,* 292 U. S. 398. Property held in present telephone use comes very near to defining itself. If particular situations shall develop ambiguity or doubt, the Commission will be available for clarifying instructions.

Fourth: The evidence does not show that the expense of revising the accounts will lay so heavy a burden upon the companies as to overpass the bounds of reason.

The decree should be affirmed, and it is

So ordered.

A true copy.

Test:

Clerk, Supreme Court, U. S.